OVERVIEW

We are one of the leading pharmaceutical retailers and distributors in Northeast China. We also have the largest pharmaceutical retail chain[(1)] and are the largest privately-owned pharmaceutical distributor[(2)] in Northeast China. According to NFS, the pharmaceutical sales of Northeast China accounted for approximately 7.1% of the total pharmaceutical market sales of China in 2012.

During the Track Record Period, we maintained rapid growth in revenue and gross profit. From 2010 to 2012, our retail and distribution revenues grew at a CAGR of 53.6% and 73.1%, respectively. According to NFS, such growth rates were the highest among all leading pharmaceutical retailers and distributors operating in Northeast China during the same periods.

We believe that both organic growth and strategic business acquisitions of our retail and pharmaceutical distribution businesses have contributed to our rapid growth during the Track Record Period:

(i) our total revenue increased from RMB858.6 million in 2010 to RMB2,326.3 million in 2012 and reached RMB1,457.0 million for the six months ended 30 June 2013;

(ii) the number of our self-operated retail pharmacies grew from 185 at the beginning of the Track Record Period to 794[(3)] as at the Latest Practicable Date; and

(iii) our distribution network expanded into a nationwide network covering approximately 3,702 customers as at the Latest Practicable Date.

We believe that our Direct-supply Model, as well as our experience in identifying and acquiring potential high-growth targets and integrating our acquired businesses have given us a competitive edge over our competitors.

For our retail business, we have 794 self-operated pharmacies, and we have achieved rapid growth through offering value-added services to our customers, providing training in our Jintian Institute and carrying out various promotion events. We also plan to launch an e-commerce pharmaceutical retail business through a third-party internet service provider by the end of 2014.

For our distribution business, our business model consists of both traditional distribution and Direct-supply Model. We are focusing on expanding our Direct-supply Model, which we believe has great development potential in China's pharmaceutical industry. According to NFS, it also allows us to achieve a profit margin which is higher than the industry average.

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(1) According to NFS, we had the largest pharmaceutical retail chain in Northeast China in terms of the number of self-operated retail pharmacies and we were the largest privately-owned pharmaceutical retail chain in Northeast China in terms of revenue in 2012.

(2) According to NFS, other than manufacturers engaging in distribution of self-manufactured products, we were the largest privately-owned pharmaceutical distributor in Northeast China in terms of revenue in 2012.

(3) This includes 279 self-operated pharmacies which were converted from contracted pharmacies during the Track Record Period but excludes four joint venture retail pharmacies which we do not control and the 15 supermarkets in Shenyang which sell healthcare products in addition to consumer goods. 574 of these pharmacies were acquired by us during the Track Record Period. We also opened 58 new pharmacies and closed 25 pharmacies during the Track Record Period.

The following table sets out the revenue and gross profit of our retail and distribution businesses during the Track Record Period.

	Year ended 31 December						For the six months ended 30 June			
	2010	% of total	2011	% of total	2012	% of total	2012	% of total	2013	% of total
	(RMB'000)		(RMB'000)		(RMB'000)		(RMB'000) (unaudited)		(RMB'000)	
Revenue										
Retail[(i)]	386,419.6	45.0	526,074.8	35.7	912,202.5	39.2	368,519.0	37.8	700,795.4	48.1
Distribution	472,193.2	55.0	947,826.9	64.3	1,414,089.4	60.8	606,014.4	62.2	756,194.5	51.9
TOTAL REVENUE	**858,612.8**	**100.0**	**1,473,901.7**	**100.0**	**2,326,291.9**	**100.0**	**974,533.4**	**100.0**	**1,456,989.9**	**100.0**
Gross Profit										
Retail	147,751.9	61.6	193,920.9	51.3	319,830.2	58.6	129,914.9	56.9	269,094.5	70.1
Distribution	91,989.3	38.4	184,223.2	48.7	225,938.4	41.4	98,235.4	43.1	114,621.4	29.9
TOTAL GROSS PROFIT	**239,741.2**	**100.0**	**378,144.1**	**100.0**	**545,768.6**	**100.0**	**228,150.3**	**100.0**	**383,715.9**	**100.0**

Note:

(i) Retail revenue for our Group does not include revenue for our contracted retail pharmacies or joint venture retail pharmacies.

We have significant competitive advantages in our home market, Northeast China. We believe that, as a market leader and pioneer, we are well positioned to benefit from the growth potential in Northeast China and the PRC in general, and from the on-going market consolidation in the PRC pharmaceutical and healthcare industry.

COMPETITIVE STRENGTHS

We have a leading position in the Northeast China pharmaceutical industry.

According to NFS, we had the largest pharmaceutical retail chain in Northeast China in terms of the number of self-operated retail pharmacies and we were the largest privately-owned pharmaceutical retail chain in Northeast China in terms of revenue in 2012. Other than manufactures engaging in distribution of self-manufactured products, we were also the largest privately-owned pharmaceutical distributor in Northeast China in terms of revenue in 2012 according to NFS. With a population of 109.7 million and without a significant presence of any national pharmaceutical retail and distribution giants, Northeast China has demonstrated a GDP per capita growth rate[(1)] which are higher than the national average pharmaceutical retail sales growth rate[(2)] from 2008 to 2012 and which in turn provide us with a favourable environment for growth.

(1) According to NFS, the CAGR for pharmaceutical retail sales from 2008 to 2012 for Northeast China was 18.1% as compared to the national average of 15.0% for the same period.

(2) According to NFS, the CAGR for GDP per capita from 2008 to 2012 for Heilongjiang, Jilin and Liaoning was 13.2%, 16.6% and 16.0%, respectively, all of which were higher than the national average of 12.9%.

We believe that the demand for pharmaceutical and healthcare products in Northeast China and the PRC in general will continue to grow as a result of the ageing population, urbanisation, increasing medical insurance coverage and increasing efforts in preventing chronic diseases in the PRC. Our leading market position, more than 15 years of operational experience and in-depth understanding of the needs and preferences of our customers in Northeast China will allow us to grow and continue to maintain our leading position in this region.

We have the ability to generate high profit margins.

According to NFS, we have a higher net profit margin than our industry peers. In 2010, 2011, 2012 and the six months ended 30 June 2013, our net profit margin was 14.3%, 12.8%, 9.8% and 11.3%, respectively. Our high net profit margin is mainly attributed to the following factors:

Our product mix: Our product mix contains High-gross-margin Products, which comprise Licensed Products and products for which we have obtained exclusive distribution rights. These products generally generate higher gross margins than other products. Sales of our High-gross-margin Products accounted for 34.3%, 34.5%, 28.0% and 25.2% of our revenue in 2010, 2011, 2012 and the six months ended 30 June 2013, respectively. The gross profit of such High-gross-margin Products accounted for 53.0%, 59.9%, 52.4% and 36.8% of our gross profit for the same periods, respectively.

Our Direct-supply Model: Our Direct-supply Model enables us to eliminate intermediaries, streamline our distribution and supply chain, and enhance the efficiency and profitability of the distribution of our products. Please see *"– We have implemented an effective Direct-supply Model"* for further details regarding this business model.

Our centralised procurement platform: We process all procurement requests within our Group through a centralised procurement platform, which allows us to leverage our economies of scale and maximise our bargaining power with suppliers to lower our procurement costs. We also help manufacturers with their procurement needs by facilitating and consolidating their procurement needs in order to obtain raw materials needed from upstream suppliers at a favorable wholesale rate due to economies of scale.

Our low operating costs: We benefit from the low rental and labour costs in Northeast China as compared to the first-tier cities in China. As such, we are able to maintain relatively low operating costs.

We have strong execution capability for acquisitions and integration.

Historically, strategic acquisitions have been the most efficient method for our expansion. We began our acquisitive expansion in 2011 and acquired 574 retail pharmacies and three pharmaceutical distribution companies during the Track Record Period. Companies acquired by us during the Track Record Period contributed 23.9%, 7.9% and 0% to our total revenue in 2011, 2012 and the six months ended 30 June 2013, respectively.

Our management team has experience in identifying targets with high growth potential and integrating the acquired businesses. We are able to identify and acquire targets among our competitors and customers, as well as through trade associations for pharmaceutical retailers. To replicate our success, we implement our product mix, advanced business model and sophisticated operation procedures in the acquired businesses through training programmes provided through Jintian Institute.

To integrate the newly acquired businesses into our existing business, we retain staff and managers of the acquired businesses who demonstrate strong aptitude and enthusiasm and who are already familiar with the acquired businesses and their existing customers. We incentivise these staff and managers by making them eligible for the Group's management ranks.

To identify who should be retained, we conduct comprehensive evaluation of the staff of newly acquired businesses. We also implement a uniform employee incentive system. All retained employees also undergo training to become accustomed to the Group's corporate culture and management philosophy.

The Group's goals for the acquired companies are to achieve, among other things: (i) increased High-gross-margin Product offerings; (ii) increased brand recognition; (iii) competitive prices in the areas serviced; and (iv) elevated quality of services through deploying knowledgeable and well-trained specialists, such as pharmacists.

In order to achieve the Group's goals for the acquired companies, the Group continues to monitor newly acquired businesses, which are led by committees of highly experienced members who are deployed on-site at the acquired businesses for the first three months following the acquisitions in order to closely evaluate the integration progress. For the subsequent three months after the initial three-month period, committee members continue to monitor off-site, conduct unscheduled inspections, and develop measures to address any outstanding concerns. Managers of newly acquired businesses are subject to the same reporting requirements to higher-level managers as the Group's existing businesses.

In addition, while taking regional differences into consideration, the systems used by the acquired businesses are also incorporated into the Group's unified management systems, where possible. Such systems include financial, information technology, inventory, and capital management systems, which facilitate and streamline management of business operations and customer relationships.

We have a track record of enhancing the operational and financial performance of our acquired businesses. Based on our experience, it generally takes six months to one year for acquired businesses to achieve our targeted financial results. This enhancement is achieved through our refined product mix, training programmes and marketing activities.

We have implemented an effective Direct-supply Model.

We have implemented a Direct-supply Model to market our High-gross-margin Products. According to the analysis of NFS, our Direct-supply Model is an effective business model for China's pharmaceutical industry. This model helps us increase our profit margin and has great development potential in China's pharmaceutical industry.

Based on our Direct-supply Model, we source most of our High-gross-margin Products at highly competitive ex-factory prices directly from manufacturers. We then sell these products to consumers, hospitals, clinics and other pharmaceutical retailers. As a result, we are able to maintain a streamlined supply and distribution chain, which enables us to eliminate a large portion of the manufacturers' promotional costs and distribution costs incurred by traditional pharmaceutical value chains. This also gives us more pricing flexibility, which allows us to maintain a favourable gross margin. We also implement featured marketing measures under our Direct-supply Model, which include marketing through trade associations for pharmaceutical retailers and training programmes through Jintian Institute. Please see *"– Our Direct-supply Model"* for further details regarding the Direct-supply Model.

During the Track Record Period, sales under the Direct-supply Model were RMB218.8 million, RMB369.1 million, RMB549.0 million and RMB380.9 million in 2010, 2011, 2012 and the six months ended 30 June 2013, respectively. Such sales accounted for 25.5%, 25.0%, 23.6% and 26.1% of our revenue and 36.1%, 38.0%, 32.4% and 38.4% of our gross profit in the same periods, respectively.

Our experienced management team has a proven track record.

We have grown from a local pharmaceutical distributor to a leading pharmaceutical retailer and distributor in Northeast China. Our success has been led by our experienced, goal-oriented and stable management team with a proven track record in China's pharmaceutical industry.

Mr. Jin, our Chairman, has over 20 years of experience in the pharmaceutical industry, with extensive knowledge of business management, marketing and strategic planning. Members of our senior management team have, on average, over 10 years of experience in the pharmaceutical industry in China. Many of our senior management team members have been with us since our inception. Through our growth and expansion, our management team has gained the experience and execution skills required to deliver continued growth and profitability. Supported by our highly-motivated and well-trained workforce, we believe that the vision and experience of our management team will continue to drive us forward.

BUSINESS STRATEGIES

We plan to continue our expansion in Northeast China and to explore opportunities in the Greater China Region.

We believe that we are well-positioned to take advantage of the significant growth potential in Northeast China and the PRC in general. We intend to further strengthen our leading market position and profitability by:

- focusing our retail expansion in Northeast China and exploring expansion opportunities in the Greater China Region. We plan to open ten self-operated retail pharmacies in the PRC and seven self-operated retail pharmacies in Hong Kong by the end of 2014. The budgeted initial costs (excluding working capital requirements) for a self-operated retail pharmacy, including the costs for the purchase of fixed assets, decoration, prepaid rent and inventory, are expected to be approximately RMB5.0 million in the PRC and approximately RMB9.6 million in Hong Kong. Our Directors believe that the net proceeds from the Global Offering will be sufficient to cover the costs of our planned expansion. Any deficiency in funding such expansion will be financed by our internal funds as appropriate;

- continuing to improve the performance and operating profit margins of our acquired retail pharmacies and distribution subsidiaries;

- expanding our distribution network in the PRC and upgrading our existing, and establishing additional, logistics centres in China;

- monitoring changing market trends and customer preferences in order to diversify and adjust our retail and distribution product portfolio and introduce suitable new brands and products under our Direct-supply Model;

- utilising our platform in Hong Kong to introduce suitable high-end products into the PRC; and

- planning to launch an e-commerce pharmaceutical retail business through a third-party internet service provider. This involves establishing a subsidiary to conduct the e-commerce business, outsourcing the development of the e-commerce system, improving our current inventory management, integrating with the Delivery Hotline 96321 system and cooperating with well-established online shopping platforms to leverage on the high traffic on such websites for our online sales and marketing. Regulatory approvals required for the e-commerce business include the subsidiary obtaining an internet medicine dealership certificate (互聯網藥品交易服務資格證書) and the internet service provider obtaining an internet medicine information service certificate (互聯網藥品信息服務資格證書) from the provincial food and drug administration, as well as a value-added telecom service operation licence from the relevant provincial communications administrator. We and the internet service provider we have selected have obtained such licences. We believe the e-commerce business will increase our retail revenue, enhance our market position and brand awareness, and extend our current retail network.

We will continue to seek acquisition opportunities.

Based on our leadership position in Northeast China and our strong acquisition execution skills, we believe that we are well-positioned to take advantage of the ongoing market consolidation in the PRC pharmaceutical and healthcare industry.

We intend to prioritise our pharmaceutical retail targets based in Northeast China and will continue to seek suitable targets in other areas in the PRC and Hong Kong to further expand our geographical coverage and product portfolio. We believe that we will be able to identify and acquire suitable targets among our competitors and customers. Mr Jin's important positions in pharmaceutical associations in the PRC allow him to gain an in-depth understanding of the industry's participants, and we have also developed an in-depth understanding of the industry's participants through our distribution business and the training programmes offered by the Jintian Institute. We believe that information gained and connections developed through such ways are useful for us to identify suitable acquisition targets and conduct effective acquisition negotiations.

In identifying suitable acquisition targets, we take into account factors including their geographical locations, product portfolios, revenues, customer base whether they complement the Group, whether their brands are sufficiently influential in their respective regions and whether their top management is capable of further growing the business.

Jintian Institute will continue to support our acquisition strategy by helping to implement our advanced business model and our comprehensive operation procedures in our acquired businesses. It will also help us maintain a talented employee base to manage and integrate our acquired businesses into our existing businesses.

We will further implement our Direct-supply Model.

We believe that further implementation of our Direct-supply Model in our operations will allow us to stay competitive and to continue to achieve a net profit margin which is higher than the industry average. In particular, we plan to:

- further increase our sales under our Direct-supply Model, especially in relation to our Licensed Products;

- continue to introduce new brands and products under our Direct-supply Model, especially in relation to healthcare products, which are increasingly popular among consumers and generally have higher gross margins than pharmaceutical products;

- further increase our influence in trade associations for pharmaceutical retailers and enhance our efforts to participate in and sponsor events organised by trade associations to increase our sales;

- enhance our leading position in the pharmaceutical industry in Northeast China by continuing to build strong brand recognition, which in turn would attract more manufacturers to participate in our Direct-supply Model;

- maintain and strengthen our relationships with suppliers and customers by continuing to improve and diversify our value-added services such as training programmes through Jintian Institute to manufacturers and customers under our Direct-supply Model. Our value-added services mainly include products and sales planning, branding, training and promotional activities, which increase brand awareness, and together with our marketing events, would expand our Direct-supply Model and allow us to offer more competitive pricing; and

- increase our efforts to promote our Licensed Products and Licensed Brands. For example, we intend to launch an advertisement campaign to promote a number of our Licensed Products and organise marketing events to raise awareness of our Licensed Brands.

We plan to increase our brand awareness and member base.

We will continue to promote our core retail brand “Jintian Aixin” by increasing our promotional efforts in the PRC. We will continue our marketing and corporate social responsibility events, such as the Jintian Exercise Program, which we believe are helpful to expand our member base. We believe that these community-focused events will continue to promote a healthy lifestyle among our existing and potential customers and enhance our corporate image. We aim to build our “Jintian Aixin” brand into a well-known retail pharmacy brand in the PRC.

To expand our member base, we will continue to promote our membership programme through various marketing events. We also plan to enhance our analysis of the consumption patterns and preferences of our members to optimise our retail marketing strategies. We will continue to diversify and improve the value-added services provided to our members. In particular, we intend to enlarge the geographical coverage of the free delivery services provided to our members under our Delivery Hotline 96321.

RETAIL BUSINESS

As at the Latest Practicable Date, we had 791[(1)] retail pharmacies in Northeast China and three retail pharmacies in Hong Kong, all of which were self-operated. During the Track Record Period, we expanded our retail network through organic growth and acquisitive expansion. We acquired 574 retail pharmacies and opened 58 new retail pharmacies during the Track Record Period. Our CAGR for our retail revenues from 2010 to 2012 was 53.6%.

During the Track Record Period, we had both self-operated and contracted retail pharmacies. The following table provides a summary of historical data of our self-operated pharmacies:

	As at 31 December			As at 30 June
	2010	2011	2012	2013
Number of pharmacies at the beginning of the period	187	185	431	600
Acquired pharmacies during the period	18	216	148	192
Pharmacies closed	(24)	Nil	Nil	(1)
New pharmacies opened during the period	4	30	21	3
Number of pharmacies at the end of the period	185	431	600	794

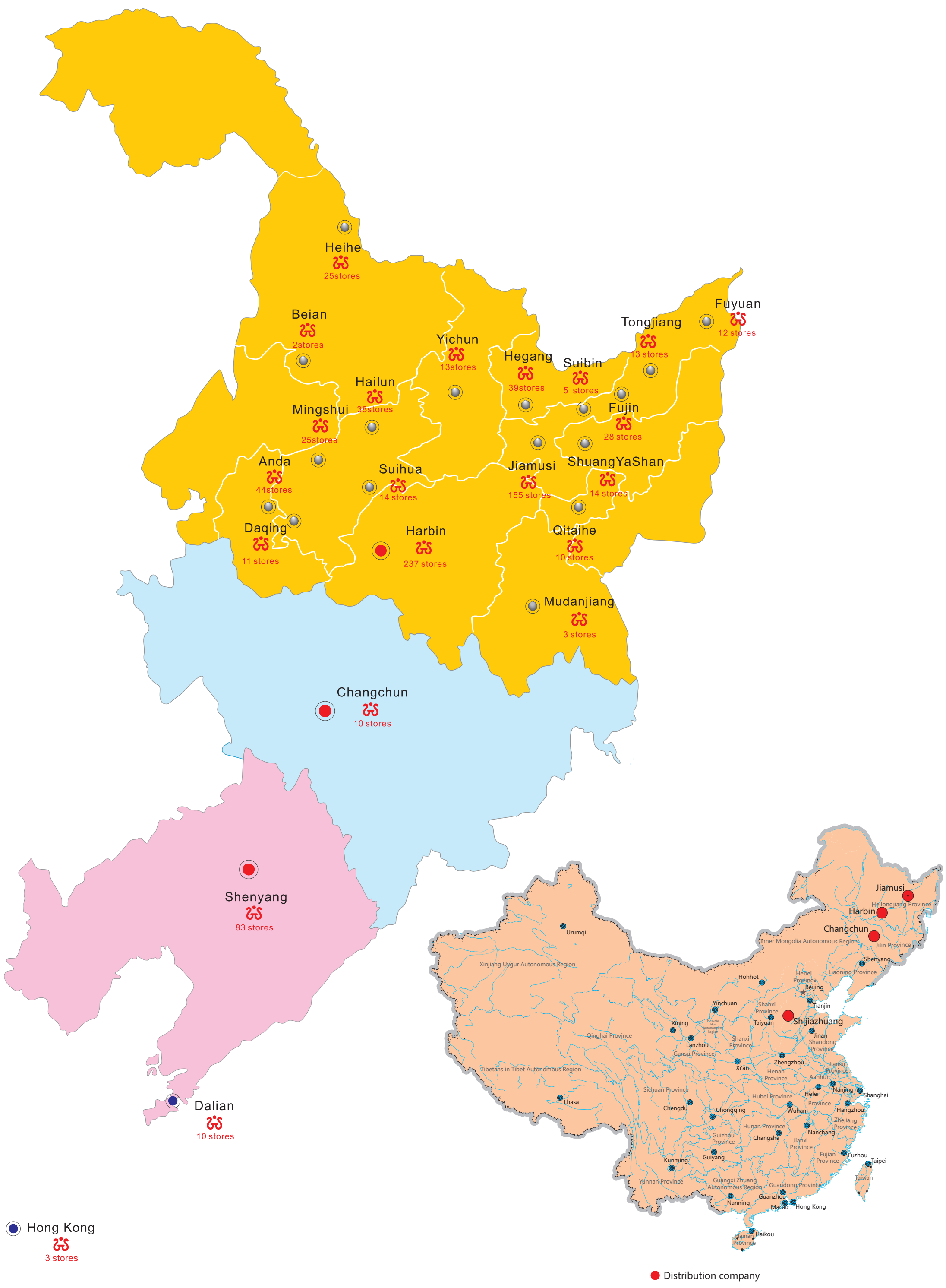
In addition to our retail pharmacies, we established 15 supermarkets in Shenyang in 2013 which sell healthcare products and consumer goods.

Revenue from our retail business amounted to RMB386.4 million, RMB526.1 million, RMB912.2 million and RMB700.8 million in 2010, 2011, 2012 and the six months ended 30 June 2013, respectively. Retail business accounted for 45.0%, 35.7%, 39.2% and 48.1% of our revenue and 61.6%, 51.3%, 58.6% and 70.1% of our gross profit in the same periods, respectively.

(1) This excludes four joint venture retail pharmacies which we do not control and the 15 supermarkets in Shenyang which sell healthcare products and consumer goods.

Our retail network

The map below illustrates our retail network as at the Latest Practicable Date.



Note:

(1) This excludes four joint venture pharmacies which we do not control.

As at the Latest Practicable Date, we had 688[1] pharmacies in Heilongjiang, 93 pharmacies in Liaoning and 10 pharmacies in Jilin.

The table below sets out the number of our pharmacies in different tiers of cities in Northeast China as at the dates indicated:

	Number of pharmacies as at the Latest Practicable Date	Number of pharmacies as at 31 December			Number of pharmacies as at 30 June
		2010	2011	2012	2013
Second-tier cities[(i)]	339	13	74	210	339
Third-tier and fourth-tier cities and towns[(ii)]	452	172	357	390	452
Total	**791**[(iii)]	**185**	**431**	**600**	**791**[(iii)]

Notes:

(i) Second-tier cities: Shenyang (瀋陽), Harbin (哈爾濱), Changchun (長春) and Dalian (大連)

(ii) Third-tier and fourth-tier cities and towns: Daqing (大慶), Mudanjiang (牡丹江), Qiqihaer (齊齊哈爾), Jiamusi (佳木斯), Suihua (綏化), Boli (勃利), Hegang (鶴崗), Shuangcheng (雙城), Suibin (綏濱), Yichun (伊春), Anda (安達), Mingshui (明水), Hailun (海倫), Beian (北安), Heihe (黑河), Fuyuan (撫遠), Shuangyashan (雙鴨山) and Qitaihe (七台河)

(iii) This excludes four joint venture retail pharmacies which we do not control and 15 supermarkets in Shenyang which sell healthcare products in addition to consumer goods.

We focus on increasing our presence in third-tier and fourth-tier cities, as we believe they possess greater growth potential and incur lower costs.

Hong Kong

In December 2012, we expanded our retail business to Hong Kong, where we acquired a pharmacy and opened two new pharmacies located in the prime retail locations of Tsim Sha Tsui and Mongkok in Kowloon. We believe that our operations in Hong Kong will play an important role as our liaison between domestic and international markets. Through our operating subsidiary in Hong Kong, we aim to approach internationally well-known pharmaceutical and healthcare product suppliers and introduce suitable high-end pharmaceutical and healthcare products into the PRC market. We have also obtained an Import and Export Goods Declaration Shipper Registration Certificate (進出口貨物收發貨人報關註冊登記證書) in the PRC to facilitate the above.

(1) This excludes four joint venture retail pharmacies which we do not control and 15 supermarkets in Shenyang which sell healthcare products in addition to consumer goods.

Retail operations

Store branding

For our retail operations, we have adopted different brands for our pharmacies at different geographical locations. These brands include "Jintian Aixin (金天愛心)", "Weikang (維康)", "Xinshiji (新世紀)", "Jintian Laobaixing (金天老百姓)", "Ciji (慈濟)", "Jishitang (濟世堂)", and "Fuhejitai (福合吉泰)". Going forward, we aim to brand all our retail operations with our core retail brand "Jintian Aixin (金天愛心)". We are in the process of implementing a uniform and distinctive layout, colour scheme and design specification in all of our pharmacies. We believe that branding all of our pharmacies with our core retail brand, "Jintian Aixin (金天愛心)", will be a very effective promotional channel and will enhance our reputation and consumer awareness. As at the Latest Practicable Date, we had completed this process with approximately 10% of our pharmacies.

Our pharmacies

As at the Latest Practicable Date, we had 794[1] pharmacies in total, all of which were self-operated. As we focused more on the acquisition of contracted pharmacies and have acquired almost 200 contracted pharmacies in 2013, we only established three new pharmacies in 2013.

Retail Pharmacy under "Jintian Aixin" brand

(1) This excludes four joint venture retail pharmacies which we do not control and the 15 supermarkets in Shenyang which sell healthcare products in addition to consumer goods.

Retail Pharmacy of Sui Hua

Internal Image of our Retail Pharmacy

We divide our pharmacies into the following categories and allocate our resources accordingly:

	Locations/Pharmacy type	Floor areas (approximately)	Products offered
Class A	Flagship pharmacies located in prime locations in Heilongjiang, Liaoning and Hong Kong	over 200 sq.m.	5,000 types of products on average
Class B	Mid-size pharmacies located in major residential neighbourhoods, prime retail locations and locations close to major hospitals and clinics in Northeast China	100 sq.m. to 200 sq.m.	3,500 types of products on average
Class C	Community pharmacies	less than 100 sq.m.	2,500 types of products on average

Contracted pharmacies

We had 143, 206 and 172 contracted pharmacies as at 31 December 2010, 2011 and 2012, respectively. As at 30 June 2013, we no longer had any contracted pharmacies in our retail network.

In the early stage of our retail expansion, we entered into agreements with our contracted pharmacy operators, who were Independent Third Parties, and granted them the rights to operate pharmaceutical retail businesses as branch offices under our retail brands.

The contracted pharmacy operators bore all costs, risks and retained earnings of the contracted pharmacies. As we did not control the operations of the contracted pharmacies, the revenue and profit of the contracted pharmacies were not consolidated into our Group. During the Track Record Period, we received RMB41.9 million, RMB83.5 million and RMB86.2 million from our contracted pharmacy operators in 2010, 2011 and 2012, respectively, most of which were payments for sourcing products from us and the rest were management fees for the provision of employee training, guidance on marketing events and guidance on product display. Such income accounted for 4.9%, 5.7% and 3.7% of our total revenue for the same periods.

As part of our expansion and development, we gradually shifted our focus from developing contracted pharmacies to self-operated pharmacies, which enabled us to better develop unified standards for various aspects of retail pharmacy operations and to provide our customers with more consistent services across our retail network. At the same time, and as part of our efforts to mitigate risks associated with our contracted pharmacy business model, we began converting our contracted pharmacies into self-operated pharmacies. Please see *"Risk Factors – Risks relating to Our Business – Historically, we did not have direct control over our contracted pharmacies and any non-compliance with applicable PRC laws and regulations by our contracted pharmacies in the past may materially and adversely affect our reputation, business, financial condition and results of operations."* for further details regarding the risks associated with our contracted pharmacy business model.

We converted 279 contracted pharmacies into self-operated pharmacies during the Track Record Period. We generally convert contracted pharmacies into self-operated pharmacies by acquiring their businesses and assets. The average consideration payable was approximately RMB0.56 million in cash for acquiring each contracted pharmacy, and it usually takes us around six months to integrate each newly acquired contracted pharmacy into our operation and achieve rapid growth accordingly. For a selection of the contracted pharmacies which we did not choose to acquire, we negotiated with the contracted pharmacy operators to terminate the business operations of such pharmacies. We believe that the termination of the contracted pharmacy business model does not have a material effect on our operations and performance.

Our supermarkets

As at the Latest Practicable Date, we had 15 supermarkets in total, all of which were located in Shenyang. The supermarkets are operated under the "Jintian Aixin (金天愛心)" brand, and are each named "Jintian Aixin Life Supermarket (金天愛心生活超市)."

Each supermarket is operated side by side with one of our pharmacies, whose store manager also has control of the supermarket's management and operations. We have opened these supermarkets in Shenyang because of the local regulations in Shenyang, which prohibit pharmacies from engaging in the retail sale of certain non-pharmaceutical products, such as products for therapeutic massage and physical therapy. In other regions, we generally sell such products in our pharmacies. Our supermarkets sell a variety of products, the majority of which are daily necessities such as drinking water, toiletries, paper tissues, and other non-pharmaceutical products which we are not allowed to sell in our pharmacies in Shenyang.

Retail product portfolio

We offer our customers a wide range of pharmaceutical products (including prescription and OTC products), healthcare products, medical devices and other personal and family care products at competitive prices. We take into account the function, reputation, and popularity of products, as well as local market preferences to determine and diversify our product mix, and periodically review and adjust our product mix in response to changing lifestyles, habits, preferences and climates.

Our product selection is designed to offer quality and choices to our customers and, at the same time, achieve high gross margins. For products with the same therapeutic purpose, we usually offer different products in each of the high, medium and low price ranges. Such product mix allows our customers to compare product features and prices, and many of our customers often choose the attractively priced products. We have many High-gross-margin Products that are also attractively priced. These products are appealing to customers in third and fourth-tier cities in Northeast China who are more price-sensitive than customers in first and second-tier cities in China. In addition to our High-gross-margin Products, we also offer products that are included in the National and Provincial Medical Insurance Drugs Catalogues and the National List of Essential Drugs, as well as other highly recognised pharmaceutical products.

High-gross-margin Products

For our retail operations, we focus on the sale and promotion of High-gross-margin Products, which accounted for 29.2% of our retail revenue and 49.5% of our retail gross profit for 2012. We often display our High-gross-margin Products in prominent places in our pharmacies in order to attract customers' attention. Please see *"– Our Direct-supply Model – Our Licensed Product Portfolio"* for further details regarding our Licensed Products and "*– Distribution Business – Distribution Product Portfolio – High-gross-margin Products*" for products for which we have obtained exclusive distribution rights. The tables below set out the breakdown of revenue and gross profit of our retail product mix during the Track Record Period:

	Year ended 31 December						Six months ended 30 June			
	2010		2011		2012		2012		2013	
	(RMB'000)	% of our retail business	(RMB'000)	% of our retail business	(RMB'000)	% of our retail business	(RMB'000)	% of our retail business	(RMB'000)	% of our retail business
Revenue										
Licensed Products	43,080.8	11.2	45,113.5	8.6	66,008.3	7.2	23,936.0	6.5	47,710.2	6.8
Products with exclusive distribution rights	65,102.1	16.8	113,044.8	21.5	200,355.4	22.0	84,747.7	23.0	108,037.8	15.4
Other products	278,236.7	72.0	367,916.5	69.9	645,838.8	70.8	259,835.3	70.5	545,047.4	77.8
TOTAL RETAIL REVENUE	**386,419.6**	**100.0**	**526,074.8**	**100.0**	**912,202.5**	**100.0**	**368,519.0**	**100.0**	**700,795.4**	**100.0**

	Year ended 31 December									Six months ended 30 June					
	2010			2011			2012			2012			2013		
	(RMB'000)	% of our retail business	Gross margin (%)	(RMB'000)	% of our retail business	Gross margin (%)	(RMB'000)	% of our retail business	Gross margin (%)	(RMB'000)	% of our retail business	Gross margin (%)	(RMB'000)	% of our retail business	Gross margin (%)
Gross Profit															
Licensed Products	24,286.1	16.4	56.4	26,873.4	13.9	59.6	37,827.1	11.8	57.3	16,226.4	12.5	67.8	26,603.6	9.9	55.8
Products with exclusive distribution rights	40,371.7	27.3	62.0	76,248.7	39.3	67.4	120,452.7	37.7	60.1	50,441.5	38.8	59.5	67,920.7	25.2	62.9
Other products	83,094.1	56.3	29.9	90,798.8	46.8	24.7	161,550.4	50.5	25.0	63,247.0	48.7	24.3	174,570.2	64.9	32.0
TOTAL RETAIL GROSS PROFIT	**147,751.9**	**100.0**	**38.2**	**193,920.9**	**100.0**	**36.9**	**319,830.2**	**100.0**	**35.1**	**129,914.9**	**100.0**	**35.3**	**269,094.5**	**100.0**	**38.4**

We seek to introduce new High-gross-margin Products to meet changing customer preferences and to differentiate us from our competitors. In addition to our existing product offering, we intend to introduce additional products to our retail customers, especially healthcare products, which are increasingly popular among consumers and generally have higher gross margins than pharmaceutical products.

Marketing and promotion

Based on our over 15 years of operational experience in Northeast China, we have obtained an in-depth understanding of the needs and preferences of our customers. Our extensive local knowledge allows us to carry out a wide range of creative marketing events which suit local preferences. By leveraging our market position and economies of scale, we often obtain sponsorships from pharmaceutical and healthcare product manufacturers for our marketing events, which allow us to effectively promote our products and services in relation to our retail operations while maintaining relatively low marketing costs.

Membership programme

Since the launch of our membership program in 2004, we have successfully built a significant member base. Our member base grew rapidly during the Track Record Period. We had approximately 225,974 members, 319,350 members, 687,558 members and 763,172 members as at 31 December 2010, 2011, 2012 and the six months ended 30 June 2013, respectively.

Customers can apply for membership at our pharmacies or when participating in certain marketing events. Upon joining our membership programme, the members will receive membership cards, which can be used to accumulate membership points based on their purchase. Such membership cards are issued by each of our retail subsidiaries separately and may only be used in the pharmacies operated by the issuing subsidiaries. The membership card is an identification card which does not have any microchip, magnetic stripe or other information storage device. As a result, our membership cards cannot be used to make payment at any of our pharmacies. We have been advised by our PRC legal advisors, Commerce & Finance Law Offices, that our issuance of membership cards does not violate any PRC laws and/or regulations. Membership points can be used to redeem gifts. Our members also receive various discounts on purchases in our pharmacies or additional value-added services, such as free body check-ups. We believe that our membership programme has been successful in promoting customer loyalty, increasing brand awareness and generating sales at our pharmacies. The continued growth of our member base is instrumental to our long-term success.

Marketing and promotion of our retail operations

In addition to our day-to-day in-store promotions, such as in-store posters, special discounts and membership discounts, we also organise various marketing events in order to promote our retail business, promote healthy lifestyles and enhance the public perception of our brand. Examples of our featured marketing events include:

- the Jintian Exercise Program, a physical recreational programme which has attracted a large number of participants. This programme enhances public awareness of our core retail brand, "Jintian Aixin (金天愛心)", and helps us gain support from local communities;

- free medical consultations and product briefing seminars for our members, for which we cooperate with local healthcare providers. Free medical consultations consist of basic health check-ups, such as blood pressure screening, provided by our employees who have had previous training on such services or third party professionals. Prior to 2012, our free medical consultations also included basic consultations for common ailments at a limited number of pharmacies. These programmes promote a healthy lifestyle among our members and generate retail sales;

- free injection services for retail customers who purchase immunization products from our pharmacies. Such injection services are provided by certain hospitals with which our Group has entered into service agreements. Please see "*Connected Transactions – Exempt Continuing Connected Transactions – 1. Medical Services Agreement*" for further details on the free injection services;

- free delivery services for our customers in Jiamusi and Suihua through our Delivery Hotline 96321. We plan to expand the services to other cities in Heilongjiang where we have retail operations. We believe that the Delivery Hotline 96321 provides us with an additional sales channel, and at the same time, allows us to gain support from local residents; and

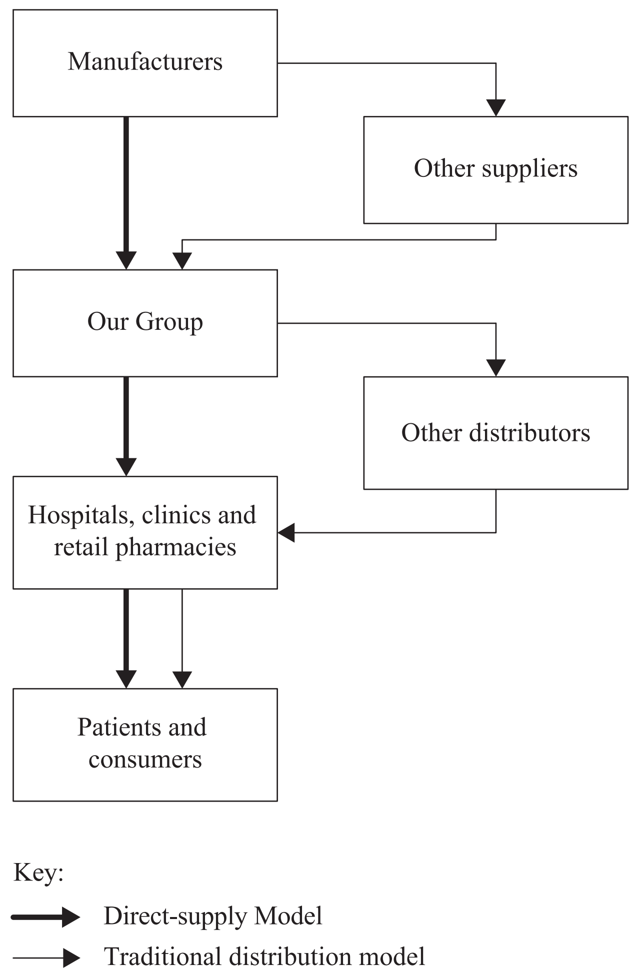
- corporate social responsibility events, including providing financial or medical assistance to local low-income families. These events help us attract media coverage and promote our brand awareness and public image.

DISTRIBUTION BUSINESS

As at the Latest Practicable Date, we had a nationwide distribution network covering approximately 3,702 customers, among which 2,554 were pharmaceutical retailers, hospitals and clinics and 1,148 were distributors. Revenue from our distribution business amounted to RMB472.2 million, RMB947.8 million, RMB1,414.1 million and RMB756.2 million in 2010, 2011, 2012 and the six months ended 30 June 2013, respectively. Distribution business accounted for 55.0%, 64.3%, 60.8% and 51.9% of our revenue, and 38.4%, 48.7%, 41.4% and 29.9% of our gross profit for the same periods, respectively.

Based on the relevant due diligence work performed, the Sole Sponsor is of the view that nothing has come to its attention that gives cause for it to reasonably believe that the significant increase in sales to distribution customers was due to accumulation of inventory on their part or the Group's sales to distribution customers were not accurate or genuine.

The following diagram illustrates the core operating process of our distribution operations:



Distribution network

Historically, we conducted our distribution operations primarily in Northeast China. Since 2005, we have extended our distribution business reach into other regions in the PRC. As at the Latest Practicable Date, our distribution network consisted of six subsidiaries and we had over 300 sales personnel. As at the Latest Practicable Date, we also had four logistics centres in Shijiazhuang, Harbin, Jiamusi and Changchun. We plan to further expand our distribution operations and upgrade our logistics centres in such locations.

Northeast China is an important market for our distribution business. Sales to our distribution customers based in Northeast China amounted to RMB325.1 million, RMB502.5 million, RMB744.2 million and RMB368.5 million, and accounted for 68.9%, 53.0%, 52.6% and 48.7% of our distribution revenue in 2010, 2011, 2012 and the six months ended 30 June 2013, respectively.

Prior to having a physical presence in other regions in China, we sold to customers located in such regions through our subsidiaries in Northeast China. The expansion of our distribution network outside of Northeast China was partly attributable to our acquisition of Hebei Yanxiao in April 2011, a company based in Shijiazhuang, which is the logistics hub of Northern China's pharmaceutical industry. Through Hebei Yanxiao, we have rapidly developed our distribution network in Northern China and Eastern China, especially in Hebei, Shandong, Shanxi and Inner Mongolia. The table below sets out the breakdown by region of our distribution revenue during the Track Record Period:

	Year ended 31 December						For the six months ended 30 June	
	2010		2011		2012		2013	
	(RMB'000)	% of our distribution revenue	(RMB'000)	% of our distribution revenue	(RMB'000)	% of our distribution revenue	(RMB'000)	% of our distribution revenue
Northeast China[(1)]	325,112.8	68,9	502,517.1	53.0	744,228.7	52.6	368,524.8	48.7
Northern China[(2)]	45,804.3	9.7	281,077.7	29.7	450,988.9	31.9	241,186.9	31.9
Eastern China[(3)]	55,328.9	11.7	80,315.2	8.5	112,920.3	8.0	63,884.4	8.4
Central China[(4)]	26,953.8	5.7	35,716.5	3.7	47,038.5	3.3	27,071.7	3.6
Northwest China[(5)]	1,457.4	0.3	20,859.2	2.2	23,410.4	1.7	18,180.6	2.4
Southwest China[(6)]	10,705.1	2.3	16,301.3	1.7	20,243.7	1.4	29,140.9	3.9
Southern China[(7)]	6,830.9	1.4	11,039.9	1.2	15,258.9	1.1	8,205.2	1.1
TOTAL DISTRIBUTION REVENUE	**472,193.2**	**100.0**	**947,826.9**	**100.0**	**1,414,089.4**	**100.0**	**756,194.5**	**100.0**

Notes:

(1) Northeast China: Liaoning, Jilin and Heilongjiang

(2) Northern China: Beijing, Tianjin, Hebei, Shanxi and Inner Mongolia

(3) Eastern China: Shandong, Jiangsu, Anhui, Zhejiang, Fujian and Shanghai

(4) Central China: Hubei, Hunan, Henan and Jiangxi

(5) Northwest China: Ningxia, Xinjiang, Qinghai, Shaanxi and Gansu

(6) Southwest China: Sichuan, Yunnan, Guizhou, Tibet and Chongqing

(7) Southern China: Guangdong, Guangxi and Hainan

Distribution product portfolio

As at 31 December 2012, our distribution portfolio consisted of over 19,000 types of products, among which 44.5% were OTC products, 32.6% were prescription products and 22.9% were healthcare products.

High-gross-margin Products

We focus on the sale and marketing of High-gross-margin Products, which accounted for 27.2% of our distribution revenue and 56.6% of our distribution gross profit in 2012. High-gross-margin Products primarily consist of our Licensed Products and products for which we have obtained exclusive distribution rights. As at the Latest Practicable Date, we distributed:

- approximately 371 types of Licensed Products to hospitals, clinics and pharmaceutical retailers under our Direct-supply Model. Other than Shan Mei Capsule (山玫膠囊), all Licensed Products were generic medicines, the formulae of which were owned by the manufacturers of such products. As at the Latest Practicable Date, 99 types of Licensed Products were prescription products and 272 types were OTC products. 32 types of Licensed Products were subject to price control policies of the PRC government. Please see "*– Our Direct-supply Model – Our Licensed Product portfolio*" for further details regarding our Licensed Products and "*Regulatory Overview – Price Controls*" for details of the price control policies of the PRC government on pharmaceutical products;

- approximately 950 types of products for which we obtained nationwide or regional exclusive distribution rights to hospitals, clinics and pharmaceutical retailers under our Direct-supply Model and to third party distributors under the traditional distribution model, among which 573 were prescription products, 349 were OTC products, 20 were healthcare products, seven were other products and one was a medical device product. All of these products were generic medicines. 256 of these products were subject to price control policies of the PRC government. Please see *"– Our Direct-supply Model"* for further details regarding our Direct-supply Model and "*Regulatory Overview – Price Controls*" for details of the price control policies of the PRC government on pharmaceutical products; and

- approximately 17,910 types of other products to distributors, hospitals, clinics and pharmaceutical retailers under our traditional business model. All of these products were generic medicines.

The following table sets out a breakdown of our revenue and gross profit generated from our distribution portfolio during the Track Record Period:

	Year ended 31 December						Six months ended 30 June			
	2010		2011		2012		2012		2013	
	(RMB'000)	% of our distribution business	(RMB'000)	% of our distribution business	(RMB'000)	% of our distribution business	(RMB'000)	% of our distribution business	(RMB'000)	% of our distribution business
Revenue										
Licensed Products	43,407.5	9.2	80,756.4	8.5	110,098.2	7.8	39,890.3	6.6	107,009.8	14.2
Products with exclusive distribution rights	142,941.4	30.3	268,895.0	28.4	274,167.0	19.4	114,537.0	18.9	104,226.3	13.8
Other products	285,844.3	60.5	598,175.5	63.1	1,029,824.2	72.8	451,587.1	74.5	544,958.4	72.0
TOTAL DISTRIBUTION REVENUE	**472,193.2**	**100.0**	**947,826.9**	**100.0**	**1,414,089.4**	**100.0**	**606,014.4**	**100.0**	**756,194.5**	**100.0**

	Year ended 31 December									Six months ended 30 June					
	2010			2011			2012			2012			2013		
	(RMB'000)	% of our distribution business	Gross margin (%)	(RMB'000)	% of our distribution business	Gross margin (%)	(RMB'000)	% of our distribution business	Gross margin (%)	(RMB'000)	% of our distribution business	Gross margin (%)	(RMB'000)	% of our distribution business	Gross margin (%)
Gross Profit															
Licensed Products	14,168.3	15.4	32.6	25,227.1	13.7	31.2	35,083.3	15.5	31.9	13,375.7	13.6	33.5	21,288.6	18.6	19.9
Products with exclusive distribution rights	48,183.4	52.4	33.7	98,252.2	53.3	36.5	92,703.5	41.0	33.8	34,192.8	34.8	29.9	25,247.1	22.0	24.2
Other products	29,637.6	32.2	10.4	60,743.9	33.0	10.2	98,151.6	43.5	9.5	50,666.9	51.6	11.2	68,085.7	59.4	12.5
TOTAL DISTRIBUTION GROSS PROFIT	**91,989.3**	**100.0**	**19.5**	**184,223.2**	**100.0**	**19.4**	**225,938.4**	**100.0**	**16.0**	**98,235.4**	**100.0**	**16.2**	**114,621.4**	**100.0**	**15.2**

As at the Latest Practicable Date, we had obtained nationwide exclusive distribution rights for 572 types of products and regional exclusive distribution rights for 378 types of products. We distribute these products under our Direct-supply Model and our traditional distribution business model, though our Direct-supply Model allows us to achieve higher profit margins compared to our traditional distribution business model.

We have obtained exclusive distribution rights for many well-known branded products in the PRC. For example, we have exclusive nationwide distribution rights for a number of products under the "Jinji" (金雞) line, a well-known gynaecologic medicine product line. We believe that by leveraging our leading position in the pharmaceutical distribution industry in Northeast China and by further developing our distribution operations in other regions of China, we will be able to expand and optimise our distribution product portfolio and to obtain more exclusive distribution rights for well-known pharmaceutical and healthcare products.

Distribution customers

The table below sets out the breakdown of our revenue generated from various categories of distribution customers, all of whom are Independent Third Parties:

	Year ended 31 December						For the six months ended 30 June	
	2010		2011		2012		2013	
	(RMB'000)	% of our distribution business	(RMB'000)	% of our distribution business	(RMB'000)	% of our distribution business	(RMB'000)	% of our distribution business
Distributors	294,918.2	62.5	468,652.0	49.4	708,537.5	50.1	321,420.2	42.5
Pharmaceutical retailers	136,479.1	28.9	283,766.3	30.0	417,703.2	29.5	342,207.7	45.3
Hospitals and clinics	40,795.9	8.6	195,408.6	20.6	287,848.7	20.4	92,566.6	12.2
TOTAL DISTRIBUTION REVENUE	**472,193.2**	**100.0**	**947,826.9**	**100.0**	**1,414,089.4**	**100.0**	**756,194.5**	**100.0**

During the Track Record Period, we maintained stable relationships with our distribution customers, some of which we have been working with for many years. The following table sets out the number of distribution customers and the associated turnover during the Track Record Period:

	Year ended 31 December			For the six months ended 30 June
Distribution Customers	**2010**	**2011**	**2012**	**2013**
At the beginning of the period	591	760	3,628	3,494
Added during the period	180	2,893	170	182
Terminated during the period	(11)	(25)	(304)	(0)
Total at end of the period	**760**	**3,628**	**3,494**	**3,676**

We experienced a significant increase in distribution customers in the year 2011 due to the acquisition of Hebei Yanxiao which had more than 2,000 customers. The acquisition of Hao Yao Shi and our own efforts to develop our business also contributed to such growth. We terminated the contractual relationship with 304 distribution customers in 2012 because our annual evaluation of the customers in terms of sales, timely settlement and transport costs revealed that these customers have fallen below our acceptable operating standards, and that the termination of such contractual relationships was in our best interest.

We have a seller/buyer relationship with our distribution customers (including distributors, pharmaceutical retailers, hospitals and clinics), and generally enter into standard and binding framework distribution agreements with them, which specify terms such as delivery, payments and purchase incentives. These standard distribution agreements generally have a term of one to three years and may be renewed by mutual agreement upon expiration. We may cease supplying if the distribution customers fail to pay us on time, or in relation to our High-gross-margin Products, fail to comply with our pricing policy by, for example, reselling our products at prices lower than our specified resale or the minimum retail prices. Pursuant to these distribution agreements, our distribution customers submit purchase orders to us from time to time, specifying products, quantity and delivery requirements. We do not fix distribution prices under these distribution agreements. Prices are generally determined through negotiations with our customers and based on market conditions. Pursuant to agreements with our distribution customers, we are generally required to provide products which meet the quality standard set by the relevant regulatory authorities. We are also responsible for the delivery of products to our customers. Our distribution customers are usually responsible for the storage, onward sale and delivery of the delivered products. Our distribution agreements generally do not provide for sales/inventory reporting requirements and obsolete stock arrangements.

In order to avoid intense competition among our distribution customers, we generally specify the resale or the minimum retail prices for our High-gross-margin Products, and restrict the geographical regions for resale. However, we generally do not set an initial purchase volume or a minimum purchase volume for our distribution customers, with the exception of hospitals whose annual purchase requirements are fixed and who usually require longer credit periods than other types of distribution customers. We believe that our practice is in line with that of other pharmaceutical distributors.

To mitigate the potential risk of competition and cannibalisation between the Group's retail sales and sales through distribution customers, the Group considers a number of factors before selecting a distribution customer. For example, the Group will take into account the geographical coverage of the end customer of our distribution customers, and will generally aim to achieve a certain distance between the geographical locations of the Group's retail customers and those of the Group's existing distribution customers.

We also provide incentives in the form of sales rebates to our distribution customers for achieving or exceeding sales targets stipulated in our distribution agreements. These targets are negotiated and determined by reference to various criteria, including past performance and market conditions. In 2010, 2011, 2012 and the six months ended 30 June 2013, our sales rebates to our distribution customers totalled RMB5.7 million, RMB6.1 million, RMB6.6 million and RMB2.4 million, respectively.

We offer most of our distribution customers a credit period up to 90 days. In determining these credit periods, we typically take into account our marketing policies and the credit histories and reputations of our customers. Each of our customers' credit limit is reviewed at the end of each calendar year.

In 2010, 2011, 2012 and the six months ended 30 June 2013, revenue from our five largest customers, which were distributors and hospital customers, in aggregate, accounted for 2.7%, 3.1%, 3.8% and 1.5%, respectively of our total revenue. During the same periods, revenue from our largest customer, which was also our largest distribution customer in 2010 and 2012 and our largest hospital customer in 2011 and the six months ended 30 June 2013, accounted for 0.9%, 0.7%, 1.0% and 0.5%, respectively of our total revenue. As at the Latest Practicable Date, none of our Directors or any of their respective associates had any interest in any of our five largest customers and we did not have any outstanding material disputes with any of our existing distribution customers.

OUR DIRECT-SUPPLY MODEL

As part of our retail and distribution businesses, we have implemented the Direct-supply Model to sell and market our High-gross-margin Products, which include our Licensed Products and products for which we have obtained exclusive distribution rights. As at the Latest Practicable Date, these products included approximately 371 types of Licensed Products and approximately 950 types of products for which we had obtained exclusive distribution rights. The following table shows the breakdown of our revenues and gross profits by business model during the Track Record Period:

	Year ended 31 December						For the six months ended 30 June	
	2010	% of total	2011	% of total	2012	% of total	2013	% of total
	(RMB'000, except percentages)							
Revenue								
Retail: Direct-supply Model	135,487.1	15.8	190,731.9	12.9	252,897.9	10.9	173,006.8	11.9
Retail: Traditional distribution model	250,932.5	29.2	335,342.9	22.8	659,304.6	28.3	527,788.6	36.2
Distribution: Direct-supply Model	83,312.0	9.7	178,404.2	12.1	296,098.5	12.7	207,864.3	14.3
Distribution: Traditional distribution model	388,881.2	45.3	769,422.7	52.2	1,117,990.9	48.1	548,330.2	37.6
Sub-total for Direct-supply Model	218,799.1	25.5	369,136.1	25.0	548,996.4	23.6	380.871.1	26.1
Sub-total for traditional distribution model	639,813.7	74.5	1,104,765.6	75.0	1,777,295.5	76.4	1,076,118.8	73.9
TOTAL REVENUE	**858,612.8**	**100.0**	**1,473,901.7**	**100.0**	**2,326,291.9**	**100.0**	**1,456,989.9**	**100.0**
Gross Profit								
Retail: Direct-supply Model	64,375.3	26.8	97,081.9	25.6	126,058.1	23.1	102,526.0	26.7
Retail: Traditional distribution model	83,376.6	34.8	96,839.0	25.6	193,772.1	35.5	166,568.5	43.4
Distribution: Direct-supply Model	22,068.9	9.2	46,743.6	12.4	50,593.2	9.3	44,703.0	11.7
Distribution: Traditional distribution model	69,920.4	29.2	137,479.6	36.4	175,345.2	32.1	69,918.4	18.2
Sub-total for Direct-supply Model	86,444.2	36.1	143,825.5	38.0	176,651.3	32.4	147,229.0	38.4
Sub-total for traditional distribution model	153,297.0	63.9	234,318.6	62.0	369,117.3	67.6	236,486.9	61.6
TOTAL GROSS PROFIT	**239,741.2**	**100.0**	**378,144.1**	**100.0**	**545,768.6**	**100.0**	**383,715.9**	**100.0**

The overall increases in sales under both the Direct-supply Model and the traditional distribution model were in line with the overall revenue growth of our pharmaceutical distribution business during these periods, which was primarily driven by (i) the expansion of our distribution network and product portfolio, (ii) more sales generated from our existing customers, and (iii) the increased overall market demand for pharmaceutical products.

During the Track Record Period, sales under the Direct-supply Model and under the traditional distribution model both achieved steady growth. Sales under the Direct-supply Model as a percentage of our total revenue amounted to 25.5%, 25.0%, 23.6% and 26.1%, respectively, and sales under the traditional distribution model as a percentage of our total revenue amounted to 74.5%, 75.0%, 76.4% and 73.9%, respectively. The fluctuation was primarily due to the concurrent growth of both models of our business. During the same periods, gross profit under the Direct-supply Model and under the traditional distribution model both recorded growth. Gross profits under the Direct-supply Model as a percentage of our total gross profit amounted to 36.1%, 38.0%, 32.4% and 38.4%, respectively, and gross profit under the traditional distribution model as a percentage of our total gross profit amounted to 63.9%, 62.0%, 67.6% and 61.6%, respectively. This was primarily because we acquired three distributors in 2011, which took time to implement our Direct-supply Model and to increase gross profit, while that under the traditional distribution model increased steadily.

Our Licensed Product portfolio

We launched our Licensed Products in 2010. As at the Latest Practicable Date, we had 371 types of Licensed Products divided into four product lines:

- (御室), the brand for our high-end modern Chinese medicines and herbal remedies, which offered 139 types of products, many of which were based on traditional Chinese medicine formulae;

- (康醫生), the brand for our high-end western medicines, which offered 82 types of pharmaceutical products targeting average retail customers;

- (社區醫生), the value brand for our Licensed Products, which offered 137 types of quality and affordable products targeting community clinics and price-sensitive customers; and

- (淘氣貓), the brand for our pharmaceutical products for children, which offered 13 types of products.

Our best-selling Licensed Products include Shan Mei Capsule (山玫膠囊), Xin An Capsule (心安膠囊), Qi Xue Shuang Bu (氣血雙補) and Bu Shen Tian Jing Wan (補腎填精丸) which are under the Yu Shi (御室) brand, as well as Flunarizine Hydrochloride which is under the Kangyisheng (康醫生) brand. Shan Mei Capsule (山玫膠囊), Xin An Capsule (心安膠囊) and Flunarizine Hydrochloride are used for the treatment of cardiovascular and cerebrovascular conditions, while Qi Xue Shuang Bu (氣血雙補) and Bu Shen Tian Jing Wan (補腎填精丸) are used for the treatment of endocrine related conditions.

Shan Mei Capsule (山玫膠囊) is a new medicine recognised by MOH. Its formula was developed by Chengde Yushi in June 1995 and is currently owned by Chengde Yushi. Shan Mei Capsule (山玫膠囊) is also recognised as a provincial-level high-tech product (省級高新技術產品) and a type of protected traditional Chinese medicine in the PRC (國家中藥保護品種).

The Controlling Shareholders, directors and senior management of the Group were not involved in the development of the Licensed Products.

We currently engage five pharmaceutical and healthcare product manufacturers, including Heilongjiang Baitai, Chengde Yushi, Mintai and Anhui Jifeng, which are our connected persons, and Huainan Jiameng Pharmaceutical Co., Ltd. (淮南佳盟藥業有限公司), which is an Independent Third Party, to manufacture our Licensed Products based on the design and packaging requirements specified by us. All of our Licensed Product manufacturers have obtained all required licences, permits and certifications, including GMP certifications.

When compared with similar products with well-known brands, most of our Licensed Products are marketed at prices which make our Licensed Products highly attractive. We only sell and market our Licensed Products under our Direct-supply Model, and as such, we do not distribute our Licensed Products to other distributors. For the years ended 31 December 2010, 2011 and 2012 and the six months ended 30 June 2013, the gross margin for the retail sale of our Licensed Products were 56.4%, 59.6%, 57.3% and 55.8%, respectively. For the same period, the gross margin for the distribution of our Licensed Products were 32.6%, 31.2%, 31.9% and 19.9%, respectively. Please see *"Financial Information – Components of Our Income Statements – Cost of Sales, Gross Profit and Gross Margin"* for further details.

We have obtained exclusive licences to use our Licensed Brands. Please see "*– Other Aspects of our Business – Our Intellectual Properties – Licensing Agreements for our Licensed Brands*" for further details regarding these licences.

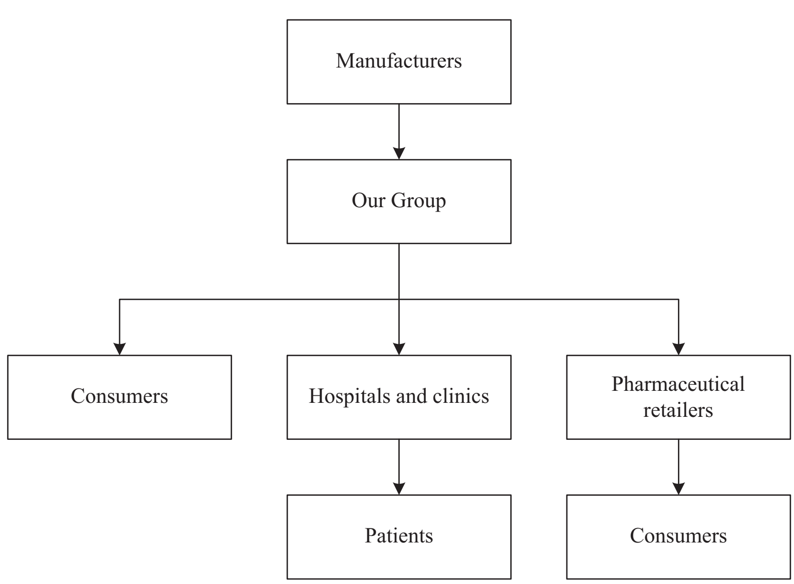
Other High-gross-margin Products we offer under our Direct-supply Model

In addition to our Licensed Products, we marketed and sold approximately 950 types of other products for which we had obtained exclusive distribution rights as at the Latest Practicable Date. Please see *"– Distribution Business – Distribution Product Portfolio"* for further details regarding these products. We also offer these products under our traditional distribution business model, but are able to achieve higher profit margins for these products under our Direct-supply Model.

Direct-supply Model and marketing

We believe that our Direct-supply Model enables us to streamline our distribution and supply chain by eliminating or reducing intermediaries and enhance distribution efficiency and profitability.

The following diagram illustrates the core operating process of our Direct-supply Model as at the Latest Practicable Date:



By leveraging our economies of scale and regional leadership position, we purchase our High-gross-margin Products at highly competitive ex-factory prices. In order to further ensure our pricing competitiveness, we also assist manufacturers of our Licensed Products with price negotiations with their raw material suppliers, as their low costs keep our procurement costs at a very competitive level.

Under our Direct-supply Model, we either directly sell our products through our retail network to customers or distribute them to hospitals, clinics and pharmaceutical retailers. We believe that under our Direct-supply Model, we are able to eliminate a large portion of the manufacturers' promotional costs and distributors' profit margins found in the traditional pharmaceutical value chain. This also gives us greater pricing flexibility, which allows us to maintain favourable gross margins. The following table sets out the breakdown of our revenue generated from our Direct-supply Model during the Track Record Period.

	Year ended 31 December						For the six months ended 30 June	
	2010		2011		2012		2013	
	(RMB'000)	% of total revenue under the Direct-supply Model	(RMB'000)	% of total revenue under the Direct-supply Model	(RMB'000)	% of total revenue under the Direct-supply Model	(RMB'000)	% of total revenue under the Direct-supply Model
Retail Total	135,487.1	61.9	190,731.9	51.7	252,897.9	46.1	173,006.8	45.4
Distribution Total	83,312.0	38.1	178,404.2	48.3	296,098.6	53.9	207,864.3	54.6
Hospitals and clinics	22,300.6	10.2	86,694.4	23.5	167,857.7	30.6	76,285.6	20.0
Pharmaceutical retailers	61,011.4	27.9	91,709.8	24.8	128,240.9	23.3	131,578.7	34.6
TOTAL	218,799.1	100.0	369,136.1	100.0	548,996.5	100.0	380,871.1	100.0

With the exception of retail sales, we conduct periodic screen customers based on their type, business scale and market position before engaging in any sales or marketing efforts in order to protect our market share and profitability. We usually only engage a certain number of pharmaceutical retailers within a geographical region as retailers for our High-gross-margin Products. We also require all of our customers not to sell our High-gross-margin Products at prices below the minimum retail prices set by us. We believe that this allows us to ensure an orderly market for our High-gross-margin Products and maintain favourable profit margins for us and the non-retail customers of our Licensed Products.

Our Directors believe that our Direct-supply Model cannot be readily imitated by our competitors, as our competitors do not possess the following competitive edges which we acquired through over 15 years of operation in the PRC pharmaceutical industry and are essential for the success of our Direct-supply Model.

Direct access to both customers and suppliers: The key element of our Direct-supply Model is direct access to both manufacturing sources and end customers. With 791 retail pharmacies in Northeast China and a nationwide distribution network, we have direct access to a large number of consumers in Northeast China and many retail pharmacies, hospitals and clinics in the PRC. Our distribution business allows us to directly approach many reputable pharmaceutical manufacturers who are able to provide us with quality products at ex-factory prices. Our centralised procurement platform attracts manufacturers, as we own the retail and distribution network and are able to coordinate and assist manufacturers with their procurement needs.

Strong marketing capability and value-added services: Our marketing activities and value-added services allow us to strengthen our relationships with our suppliers and customers under the Direct-supply Model. Our marketing activities include our Jintian Exercise Program and membership program for our retail customers, trade association seminars and conferences to facilitate direct sales to pharmaceutical retailers and training programs focusing on product features, marketing and sales techniques offered to pharmaceutical retailers through our Jintian Institute. These marketing programs not only save promotion costs of the pharmaceutical retailers, but also increase their purchasing volume with us. Another value-added service we provide to manufacturers is the facilitation of their raw material procurement, which also helps us keep our procurement costs at a competitive level. We also help manufacturers with the recruitment of talents, which we have access to and experience in identifying both technical and management potential resulting from our years of experience in the pharmaceutical industry.

Experienced and stable workforce: Another key element to our success is our experienced and stable workforce. Such workforce has grown with us and frequently attends training programs provided through Jintian Institute. Our employees are experienced in many aspects of the Direct-supply Model, such as pharmaceutical product manufacturing, procurement and quality control, pharmacy operation and marketing.

Marketing and promotion under our Direct-supply Model

Under our Direct-supply Model, we actively market and sell our products through trade associations for pharmaceutical retailers in the PRC. These trade associations are formed by small to medium-size pharmaceutical retailers which are individually less competitive, but when acting together, have stronger collective bargaining power. Through trade associations, we have gained direct access to many regional pharmaceutical and healthcare product retailers, especially in geographic regions where we do not have retail operations.

We are a core member of the China Medical and Resources Association, which is a national pharmaceutical retailer trade association with sub-associations in 19 provinces in the PRC. It covers more than 460 pharmaceutical retail chains and over 20,000 pharmacies owned by these pharmaceutical retail chains. In addition, Mr. Jin, our Chairman, also serves as a vice president of the China Medical and Resources Association and president of its sub-association in Heilongjiang. We believe that we will continue to benefit from these trade associations, in terms of generating sales under our Direct-supply Model. Also, Mr Jin's leadership positions in trade associations in the PRC allow him to gain an in-depth understanding of the industry's participants, especially in geographical locations where we do not have a physical presence. We believe that information gained and connections developed through such associations are useful for us to identify suitable acquisition targets and conduct effective acquisition negotiations.

Trade associations for pharmaceutical retailers frequently organise seminars and conferences to facilitate direct sales and purchases among pharmaceutical and healthcare product suppliers and retailers. We actively participate in and sponsor these seminars and conferences.

In addition, to increase sales under our Direct-supply Model, particularly with regard to our Licensed Products, we provide value-added training programmes through Jintian Institute to our customers and potential customers which are pharmaceutical retailers. The training programmes offered focus on product features, marketing and sales techniques and general medical and nutrition knowledge which we believe are useful to increase sales under our Direct-supply Model. Please see *"– Jintian Institute"* for further details regarding the training programmes. In order to monitor and improve our High-gross-margin Products' performance in third party pharmacies, our experienced sales personnel regularly visit these pharmacies to facilitate the in-store sale, marketing and promotion of our products.

JINTIAN INSTITUTE

The Jintian Institute is our in-house training and development centre, providing training to our employees as well as our important distribution customers. We believe that the Jintian Institute has significantly contributed to our expansion and success in the past, and distinguishes us from our competitors. Under the Jintian Institute, we provided over 90, 100 and 158 training sessions to our employees and 18, 25 and 30 training sessions to our customers and potential customers in 2010, 2011 and 2012, respectively.

Training programmes for our employees

The Jintian Institute provides systematic and comprehensive training programmes on a regular basis to our employees. These training programmes focus on improving our employees' sales skills and understanding of our corporate culture. For example, we provide an array of training programmes and courses covering various aspects of our business operations, such as medical and nutrition knowledge, store operations and procedures, sales and marketing techniques, customer interaction and service skills. We also provide training to our management team in areas such as business process and planning, leadership development, effective communication and management skills. Another key function of the Jintian Institute is to organise events and seminars to promote our corporate values, which are persistence, goal-orientation, team-work and collectivism.

Through these training programmes, our employees are able to master our standard operating procedures, communicate effectively with our customers and acquire a better understanding of our customers' preferences. The Jintian Institute also helps us build an experienced, loyal and focused workforce. In addition, we are able to strengthen our talent pool at different levels of seniority, which is the foundation of our growth and expansion. These training programmes also encourage our employees to advance their careers with us.

Training programmes provided to our customers and potential customers

As an effective marketing tool, the Jintian Institute also offers training to customers and potential customers of our High-gross-margin Products. We aim to increase sales of our High-gross-margin Products through these training programmes. We believe that these programmes help us maintain mutually-beneficial relationships with our customers and promote our corporate image.

OUR CENTRALISED PROCUREMENT PLATFORM AND INVENTORY MANAGEMENT

Our centralised procurement platform

Product procurement is crucial to our operations. We are committed to offer our customers a wide variety of high quality pharmaceutical and healthcare products at competitive prices. We achieve this by utilising our efficient and centralised procurement platform, which is responsible for all of our retail and distribution procurement. This platform allows us to:

- leverage our economies of scale and maximise our bargaining power to lower procurement costs;

- analyse supply information and monitor price movements;
- refine our product mix to ensure our focus is on our High-gross-margin Products;
- monitor inventory levels throughout our Group and optimise inventory allocation through our computerised inventory management system; and
- select and assess our suppliers to ensure that they are reputable and reliable.

In addition, our procurement platform ensures competitive pricing for our Licensed Products. We centralise our procurement through our procurement department, which handles supplier negotiations, the placing of purchase orders and cost control. Through collecting procurement information and conducting bulk purchase of products, we are able to assist our Licensed Product manufacturers with price negotiation with their raw material suppliers, as their low costs keep our procurement costs at a very competitive level.

Inventory management

Our inventory primarily consists of a variety of pharmaceutical products, healthcare products and other products required for our retail and distribution operations. Our inventory turnover is usually stable and is determined based on our sales plans and market demands. Our computerised inventory management system allows us to track the inventory levels and the movement of products in our warehouses and self-operated retail pharmacies on a real-time basis and assess product popularity. Based on such information, we are able to adjust our distribution and marketing strategies. We monitor the shelf life of the products in our warehouses and self-operated retail pharmacies. When certain products are found to be slow-moving or close to expiry, we generally will launch promotions to encourage the sales of such products. We typically dispose of expired products, which are written off accordingly. In 2010, 2011, 2012 and the six months ended 30 June 2013, our average inventory turnover days were approximately 45.8 days, 42.5 days, 43.2 days and 43.6 days, respectively.

OTHER ASPECTS OF OUR BUSINESS

Suppliers

We focus on streamlining our supply chain to lower our procurement costs. As a result, we endeavour to source directly from manufacturers as much as possible. If we cannot purchase from manufacturers directly due to exclusive distribution rights held by third parties, we endeavour to source from first-tier distributors. For example, we purchase from manufacturers directly for all of our Licensed Products and products for which we have obtained national exclusive distribution rights. As at the Latest Practicable Date, we had 854 suppliers which were manufacturers and 523 suppliers which were distributors. In 2010, 2011 and 2012, 50.3%, 42.0% and 34.4% of our product procurement was sourced directly from manufacturers, respectively.

Our supply agreements with most of our suppliers, including supply agreements for our Licensed Products and products for which we obtained exclusive distribution rights, are for a term ranging from one to five years. A portion of our supply agreements may specify purchase commitments, depending on the individual suppliers. The Group had met its purchase commitments under such supply agreements during the Track Record Period. Some of our supply agreements may contain price terms, but prices are generally determined through negotiations with our suppliers and based on market conditions. We have not entered into any hedging arrangements to manage fluctuations in the prices of supplies. Our Directors believe that our ability to pass on significant increases in the cost of supplies will depend on market conditions.

In particular, the supply agreements for products for which we obtained exclusive distribution rights, including those with connected persons, are usually for a term ranging from one to three years. The expiry dates of such exclusive supply agreements currently in force range from 31 December 2013 to 31 December 2016. The exclusive supply agreements would specify the region for our exclusive distribution rights, and typically include a minimum purchase requirement and/or a minimum resale target for each year in terms of money value. The agreements usually have terms as to the pricing and resale policies, as well as maintenance of brand image and product quality. We have the obligation to re-sell in accordance with such pricing and resale policies and to maintain the brand image and product quality for the suppliers. We are sometimes required to maintain the inventory for particular types of products above a specified minimum level. The suppliers have the right to introduce new distributors into the region if we breach such minimum inventory requirement. The agreements would also usually specify a time period for return of products in the absence of product quality issues, ranging from 30 to 60 days. Where products are defective or there are problems with product quality, such products can be returned at any time. Termination clauses usually include events such as non-compliance with the agreed distribution territory restrictions or the agreed resale policy, and the Group causing serious damage to the suppliers' brand image such as selling counterfeit products. The obligations to ensure product quality are borne by the suppliers.

We believe that alternative suppliers or alternative products are readily available for substantially all of the products we sell, and the loss of any individual supplier would not have a material effect on our operations. We have not experienced significant difficulties in maintaining reliable sources of supplies, and we generally expect to be able to maintain adequate sources of supplies for our retail and distribution operations.

Purchases from our top five suppliers accounted for 19.9%, 12.2%, 13.0% and 15.1% of our total purchases in 2010, 2011, 2012 and the six months ended 30 June 2013, respectively. Purchases from our largest supplier accounted for 5.7%, 3.3%, 3.2% and 4.5% of our total purchases in the same periods, respectively. Save for the following, none of our Directors or any of their respective associates or, so far as our Directors were aware, any Shareholder who owned 5% or more of our issued share capital as at the Latest Practicable Date, had any interest in any of our five largest suppliers in 2010, 2011, 2012 and the six months ended 30 June 2013:

- Heilongjiang Baitai was one of our five largest suppliers throughout the Track Record Period. On 28 April 2012, Ms. Liu Shuxia (劉樹霞), Mr. Jin's cousin-in-law, acquired 100% of the equity interest in Heilongjiang Baitai. Our total purchases from Heilongjiang Baitai amounted to RMB34.9 million, RMB36.6 million, RMB54.2 million and RMB25.1 million in 2010, 2011, 2012 and the six months ended 30 June 2013, respectively. During the same periods, purchases from Heilongjiang Baitai accounted for 5.7%, 3.3%, 2.9% and 2.4% of our total purchases, respectively. Heilongjiang Baitai was our largest supplier in 2010 and 2011 and second largest supplier for the year ended 31 December 2012. Please see *"Connected Transactions – Non-exempt Continuing Connected Transactions and Application for Waivers – 3. National Sales and Use of Trademark Agreement with Heilongjiang Baitai"* for further details; and

- Chengde Yushi, one of our five largest suppliers during the Track Record Period, was 95% owned by Ms. Chen and 5% owned by Mr. Geng Changsheng (耿長勝), who is Mr. Jin's cousin. On 15 March 2013, Ms. Chen transferred her 95% equity interest in Chengde Yushi to Mr. Geng Liyuan (耿立元), who is Mr. Jin's uncle, also Mr. Geng Changsheng's father. Our total purchases from Chengde Yushi amounted to RMB20.8 million, RMB23.9 million, RMB46.7

million and RMB47.3 million in 2010, 2011, 2012 and the six months ended 30 June 2013, respectively. During the same periods, purchases from Chengde Yushi accounted for 3.4%, 2.2%, 2.5% and 4.5% of our total purchases, respectively. Chengde Yushi was our fourth largest supplier in 2010 and third largest supplier in 2011 and 2012. Please see *"Connected Transactions – Non-exempt Continuing Connected Transactions and Application for Waivers – 2. National Sales and Use of Trademark Agreement with Chengde Yushi"* for further details of the transactions between the Group and Chengde Yushi.

We mainly procured our Licensed Products from Heilongjiang Baitai and Chengde Yushi during the Track Record Period. Purchases from associates of the Controlling Shareholders, which are Heilongjiang Baitai and Chengde Yushi, amounted to an aggregate of RMB55.7 million, RMB60.5 million, RMB100.9 million and RMB72.4 million in 2010, 2011, 2012 and the six months ended 30 June 2013, respectively. During the same periods, purchases from Heilongjiang Baitai and Chengde Yushi in aggregate accounted for 9.1%, 5.5%, 5.3% and 6.9% of our total purchases, respectively.

Risk Management

We plan to adopt a risk management policy after the Listing to manage our operational risks. Under our risk management policy, our key risk management objectives include:

- developing a comprehensive risk management strategy for our Company;
- recognising different types of risks and developing appropriate risk management strategies based on the type of risk;
- identifying, monitoring and managing risk and our risk tolerance level; and
- balancing risk management with the development of our Company.

Under our risk management policy, our Board is responsible for establishing the key risk management principles and objectives, while our chief executive officer is responsible for establishing risk management measures and reviewing material risks within our Company. We have established a compliance and audit department which is expected to be responsible for implementing our risk management efforts, and each of our PRC operating subsidiaries has a designated risk management department which is expected to be responsible for coordinating and supervising our risk management efforts within the subsidiary.

Anti-bribery measures

As part of our risk management and internal control measures, the Group has established a set of internal regulations against corrupt and fraudulent activities, which includes measures against receiving bribes and kickbacks, and misuse of company assets. This set of regulations applies across the Group, including our subsidiaries, and sets out the following:

- The audit department is responsible for the daily execution of the anti-bribery measures. Its scope of duties include reviewing and assessing the anti-bribery measures in each department, reviewing complaints and reports from internal and external sources, and conducting investigations and undertaking rectification actions accordingly. The audit department reports to an anti-bribery executive committee led by the chief executive officer and comprising the second-in-command of each key department.

- We have set up a system for handling complaints and investigations. We accept both named and anonymous complaints through our telephone hotline and email hotline. Both hotlines are announced and circulated to all levels of employees as well as all external parties that have direct or indirect economic relationship with the Group. For complaints that involve senior management, a special investigations team will be formed, consisting of members from the audit department and the management of the relevant department, and external investigators will be employed if necessary. The audit department ensures feedback as well as protection is provided to the whistleblower. The progress of investigations is archived accordingly, and also reflected to our Directors on a quarterly basis.

- At the beginning of each year, we conduct a risk assessment and this includes assessment of risks of bribery, false financial reports, misappropriation of company assets, and inappropriate income or expenses. The assessment is made with regard to each business department and is also conducted on major accounts, as well as each senior management member and board member.

- We ensure that all employees receive training about compliance with the relevant laws and professional ethical standards upon recruitment. Our internal regulations and policies on anti-bribery are included in staff handbooks. For any person to be employed or promoted for important positions, we also conduct background investigations, the results of which are duly recorded and archived.

- We communicate with all relevant stakeholders, including customers and suppliers, about our compliance measures and professional ethics guidelines.

- If fraudulent activities take place within the Group, we would ensure that written reports of the rectification measures are circulated internally and to external parties if necessary.

- Our senior management shall have annual meetings specifically to review the measures against bribery and other fraudulent activities. Ad-hoc meetings will also be convened when there are serious incidents, including when any general management of the headquarters, the branch offices or the subsidiaries are involved in fraudulent activities. At the meetings, each department head reports to the anti-bribery executive committee about the status of their own department, and the audit department reports about the status and progress across the Group.

The Group has implemented preventive anti-bribery measures in its daily operations. For example, price quotations for procurement obtained by an employee are independently verified by another employee to ensure that there are no discrepancies in the pricing. The Group also segregates duties of sales operation where possible, such as the making of sales, receipt of payments and maintenance of sales records, and monitoring sales by managing the sales process via a computerised system which keeps proper records of sales transactions and prices and discounts, which makes it more difficult for an employee to carry out any fraudulent activities.

Our Directors, to the best of their knowledge, confirm that during the Track Record Period and up to the Latest Practicable Date, the Group and its employees were not involved in any bribery activities or under investigation by relevant authorities in relation to bribery.

Quality control and product liability

We are committed to providing quality products to our customers, and we carefully select our suppliers based on various factors, including their product selection and quality, business scale and reputation. Our suppliers typically provide quality assurance, and we are able to return any goods if we become aware of any quality issues. During the Track Record Period, we had one incident of product return, which was related to defective medical capsules. The manufacturer and supplier voluntarily initiated a product recall and provided replacement capsules to us free of charge. As a result of our swift response in reaching out to our customers and addressing any questions or concerns they may have, the incident did not have a material adverse effect on our sales, results of operations, business operations or reputation. Other than this incident, we did not have any other significant incidents of product return during the Track Record Period.

All products purchased by us are inspected and examined for packaging issues and expiry dates upon arrival before acknowledging receipt. After receipt, all products are stored at our warehouses, which satisfy the GSP requirements.

In general, manufacturers of pharmaceutical and healthcare products are responsible for product liability. We may also be liable for products we have sold, especially if such liability is due to improper storage or product expiry, for which we are at fault. We have not subscribed for product liability insurance, as such liability is generally borne by the manufacturer.

Pricing

Our product pricing takes into account various factors, including our procurement and operation costs, profit margin, market competition and conditions and customer preferences. In addition, a portion of the pharmaceutical products included in the National and Provincial Medical Insurance Drugs Catalogues, National List of Essential Drugs and related legislation and regulations are subject to price controls, which in turn will affect our pricing for these products. As at 30 June 2013, 6.9% of our revenue was derived from products subject to price controls under the National or Provincial Medical Insurance Drugs Catalogues. Please see *"Regulatory Overview – Price Controls"* for further details regarding price controls.

Product return

Except for quality issues, we generally have not allowed product returns or refunds for our retail pharmaceutical products since 1 June 2013. Such policy complies with relevant PRC laws and regulations.

For our distribution business, we also generally do not allow product returns or exchanges, except if due to quality issues and specific circumstances.

During the Track Record Period, the value of returned products for our retail and distribution operations was insignificant.

Employees

For the years ended 31 December 2010, 2011 and 2012 and the six months ended 30 June 2013, we had 1,314, 2,512, 4,331 and 4,984 full-time employees, respectively. The table below sets out a breakdown of our employees by function for the periods indicated:

	Year ended 31 December						For the six months ended 30 June	
	2010		2011		2012		2013	
Function	Number of employees	% of total employees	Number of employees	% of total employees	Number of employees	% of total employees	Number of employees	% of total employees
Central and regional management	77	4.6	108	4.1	144	3.2	142	2.8
Store-level management	203	12.2	332	12.6	597	13.4	699	13.8
General administration	303	18.2	350	13.2	513	11.5	516	10.2
Sales (retail)	867	52.3	1,593	60.2	2,904	65.3	3,407	67.0
Sales (distribution)	211	12.7	261	9.9	293	6.6	317	6.2
Total	**1,661**	**100.0**	**2,644**	**100.0**	**4,451**	**100.0**	**5,081**	**100.0**

For the six months ended 30 June 2013, approximately 2.8% of our employees were central and regional management-level employees and approximately 90% of our managerial-level employees had been employed by us for over ten years.

The following table sets out a breakdown of our employees by education level for the periods indicated:

	Year ended 31 December						For the six months ended 30 June	
	2010		2011		2012		2013	
Education	Number of employees	% of total employees	Number of employees	% of total employees	Number of employees	% of total employees	Number of employees	% of total employees
Master's degree and above	4	0.2	8	0.3	8	0.2	5	0.1
Bachelor's degree	36	2.2	42	1.6	90	2.0	147	2.9
Associate degree	682	41.1	1,041	39.4	1,950	43.8	2,374	46.7
High school degree and below	939	56.5	1,553	58.7	2,403	54.0	2,555	50.3
Total	**1,661**	**100.0**	**2,644**	**100.0**	**4,451**	**100.0**	**5,081**	**100.0**

We have implemented a number of initiatives to enhance the productivity of our employees. In particular, we conduct periodic performance reviews of most of our employees, and their compensation is tied to their performance. Further, our compensation structure is designed to incentivise our employees to perform well by linking a portion of their compensation to their performance and the overall performance of our Group. The performance-based portion depends on the employee's job function and seniority.

Please see *"– Jintian Institute – Training programmes for our employees"* above for the training we provide for our employees.

Operational safety and environmental protection

Our PRC legal advisors, Commerce & Finance Law Offices, have confirmed that we have not breached, in any material aspects, any PRC laws or regulations related to operational safety and environmental protection.

Insurance

We maintain different types of insurance policies to cover our assets and operations, including insurance for our warehouses. Our Directors are of the view that our current insurance is in line with industry standards and is adequate.

Our intellectual properties

As at the Latest Practicable Date, we had eight registered trademarks and two registered domain names which were material to our business. Further details regarding our intellectual properties are set out in *"Statutory and General Information – Further information about our business – Intellectual property rights of the Group"*.

Our Directors confirm that as at the Latest Practicable Date, there had not been any material infringement on our trademarks. However, if there is any infringement on our trademarks in the future, our image and profitability may be adversely affected, and we may take action against third parties in respect of such infringement.

Licensing agreements for our Licensed Brands

We currently sell and distribute our Licensed Products under the Licensed Brands, namely, "Yushi" (御室), "Kangyisheng" (康醫生), "Shequyisheng" (社區醫生) and "Taoqimao" (淘氣貓). "Yushi" (御室) was licensed to us by Chengde Yushi; "Kangyisheng" (康醫生) was licensed to us by Heilongjiang Baitai; and "Shequyisheng" (社區醫生) and "Taoqimao" (淘氣貓) were licensed to us by Jiamusi Jinmenggongchang.

Pursuant to the trademark licensing agreements, we have the exclusive right to use and sublicense the Licensed Brands. Such licensing agreements also allow us to instruct third party manufacturers, other than the trademark owners, to manufacture products bearing such Licensed Brands without prior consent from the relevant licensors.

Each of our current trademark licensing agreements with Chengde Yushi, Heilongjiang Baitai and Jiamusi Jinmenggongchang, for which we will pay RMB8.75 million, RMB7.80 million and RMB2.95 million, respectively, became effective on 1 July 2013 for a term of three years. The licensors shall not transfer the relevant Licensed Brands to third parties without prior consent from us. In the event a Licensed Brand is transferred, the relevant licensor shall procure the transferee to enter into a trademark licensing agreement following the principal terms of the agreement between such licensor and us. These licensing agreements are renewable upon expiry at the consent of both parties and we have the right of first refusal in acquiring these Licensed Brands if the brand owners intend to sell the respective Licensed Brands.

Chengde Yushi acquired "Yushi" (御室) from Mr. Yao Yonghong (姚永紅), an Independent Third Party, in May 2007. Before "Yushi" (御室) was exclusively licensed to the Group since 30 June 2013, it was used by Chengde Yushi on its various pharmaceutical products. Chengde Yushi was established in March 2001. It engages in the business of production of pills, tablets and capsules.

Heilongjiang Baitai established "Kangyisheng" (康醫生) in June 2003. Before "Kangyisheng" (康醫生) was exclusively licensed to the Group since 30 June 2013, it was used by Heilongjiang Baitai on its various pharmaceutical products. Heilongjiang Baitai was established in July 1998. It engages in the business of production of tablets, capsules and healthcare products.

Jiamusi Jinmenggongchang acquired "Shequyisheng" (社區醫生) and "Taoqimao" (淘氣貓) from Mr. Qi Yongjun (齊擁軍), an Independent Third Party, in April 2012. Before "Shequyisheng" (社區醫生) and "Taoqimao" (淘氣貓) were exclusively licensed to the Group since 1 July 2013, they were licensed to other pharmaceutical manufacturers. Jiamusi Jinmenggongchang was established in April 2000. It engages in the business of advertisement design, production, planning and publication.

The Controlling Shareholders, directors and senior management of the Group have not been involved in the registration of the relevant trademarks associated with the Licensed Brands.

For more details on our past and current trademark licensing agreements, see "*Connected Transactions – Non-exempt Continuing Connected Transactions and Application for Waivers*."

Competition

The PRC pharmaceutical retail and distribution industry is currently highly fragmented with numerous market participants. Our Directors believe that a market consolidation is currently underway in the PRC pharmaceutical and healthcare industry. We believe that while competition will continue to increase, not all participants within the pharmaceutical retail and distribution industry can be considered our competitors due to differences in target customer bases, business models and product portfolios.

National pharmaceutical retail giants do not have a significant presence in the Northeast China pharmaceutical retail market. In relation to our retail operations, our competitors are mainly regional and local pharmaceutical retail chains operating in Northeast China. For our distribution operations, we mainly face competition from distributors who have adopted business models which are similar to our Direct-supply Model. According to NFS, these competitors including Tege'er Group (特格爾集團) based in Hunan and Golden Lily Group (金百合集團) based in Guangdong. As the Northeast China pharmaceutical market continues to grow and as we gradually expand our distribution reach in the PRC, we may face increasing competition from national pharmaceutical retail and distribution giants.

Properties

Owned property

As at the Latest Practicable Date, we owned one property located in Harbin with a total gross area of approximately 675.4 sq.m., all of which were for storage purposes. We have obtained the building ownership certificate and the related land use right certificate for this property.

As at the Latest Practicable Date, the Directors confirmed that no single property interest which forms part of our non-property activities has a carrying amount (within the meaning of the Companies Ordinance (Exemption of Companies and Prospectuses from Compliance with Provisions) Notice (Chapter 32L of the Laws of Hong Kong) (the "**Exemption Notice**") and Chapter 5 of the Listing Rules) of 15% or more of our total assets.

In light of the above, pursuant to Section 6(2) of the Exemption Notice, this prospectus is exempted from compliance with the requirements of Section 342(1)(b) of the Companies Ordinance in relation to paragraph 34(2) of the Third Schedule to the Companies Ordinance, which requires a valuation report to be prepared in respect of all our interests in land or buildings. Pursuant to Chapter 5 of the Listing Rules, this prospectus is not required to include valuations of our properties.

Leased properties

As at the Latest Practicable Date, we leased 812 properties in various cities in China and Hong Kong, with a total gross floor areas of approximately 146,490.3 sq.m. Our leased properties are used as retail pharmacies, storage and offices. The leases underlying these properties have certain defects:

(A) The lessors of 18 of these properties do not have the relevant building ownership certificates or any other title documents to prove their rights to the properties. If the lessors do not have lawful rights to these properties, we may not be able to continue to occupy and use such properties. In particular, 16 of these 18 properties were used by us as pharmacies as at the Latest Practicable Date, while the others were used as offices and warehouses. If the lessors do not have lawful rights to these properties, we may not be able to continue to occupy and use such properties. If we are required to relocate, our Directors believe that similar properties at similar locations can be easily identified.

- Before we leased these 18 properties from the relevant lessors, we had conducted necessary enquiries with such lessors and had obtained their confirmation in respect of their titles to such properties. We had also requested for the purchase agreements and payment vouchers in relation to such properties, and conducted reviews where such documents were available. As at the Latest Practicable Date, we were not aware of any actions which had been brought to challenge the title to such properties. As such, our Directors believe that, although the lessors of these 18 properties are not able to provide us with their title documents, we have taken necessary actions to support our belief that they have proper title to such properties. If we are required to relocate, our Directors believe that the time required for relocation of each property would not take more than two months.

- Our Directors believe that these 18 leased properties are not crucial to our operation, especially as the Group can relocate these pharmacies, offices and warehouses and the relocation costs will not have a material adverse impact on our operation and financial performance.

(B) None of our lease agreements have been registered with the relevant PRC authorities, which may result in correction orders by relevant authorities and may subject us to a fine of RMB1,000 to RMB10,000 per lease agreement.

- As advised by our PRC legal advisors, Commerce & Finance Law Offices, the validity of the lease agreements that were not duly registered or filed with the relevant governmental authorities is not affected by such failure to register or file. In respect of the non-registered lease agreements, correction orders may be given by the relevant governmental authorities to register the lease agreements within a prescribed period, failing which a fine ranging from RMB1,000 to RMB10,000 per lease agreement may be imposed for each unregistered lease agreement. As at the Latest Practicable Date, we had not received any such correction orders. We will proceed to register our lease agreements with the relevant PRC authorities if we receive such orders from them.

Our Directors believe that the defects with our leases will not have a material adverse impact on our operations, and are not individually or collectively crucial to our operations.

The following table sets forth the property interests rented and occupied by us as at 30 September 2013.

Business segment	Brief description of properties	Gross floor area	Usage	Dates of expiry[1]	Average effective rental charge
Retail	809 leased properties in the PRC	125,045.75 sq.m.	Retail, storage and office	Between December 2013 and December 2022	Average annual rent of approximately RMB525.3 per sq.m.[2]
	3 leased properties in Hong Kong	280 sq.m.	Retail	Between July 2014 and October 2015	Average annual rent of approximately RMB16,061.1 per sq.m.[2]
Distribution	9 leased properties in the PRC	21,164.5 sq.m.	Distribution and storage	Between April 2014 and December 2022	Average annual rent of approximately RMB251.4 per sq.m.

Notes:

(1) Approximately 90% of our lease agreements will expire around 2014 to 2016.

(2) Rental charges for leased properties under the retail segments are expressed on an annual basis at fixed rates for each retail pharmacy in the majority of the lease agreements, while the rest are expressed as a fixed amount for each retail pharmacy for the specific term of the relevant lease agreements.

As at the Latest Practicable Date, none of our lease agreements had expired.

Legal and compliance matters

As at the Latest Practicable Date, no member of our Group was engaged in any litigation, claim or arbitration of material importance, and no litigation, claim or arbitration of material importance was known to our Directors to be pending or threatened against any member of our Group.

Set forth below is a summary of our material non-compliance matters during the Track Record Period, as well as rectification actions and preventive measures that we have taken in respect of such matters, including obtaining confirmations from relevant regulatory authorities that they would not impose penalties or other measures on us.

Matters of non-compliances	Reasons, details and legal consequences of non-compliances	Rectification Actions
(A) Failure to renew medical device operation permits	Due to administrative oversight, we failed to renew the medical device operation permits for 19 of our pharmacies. The medical device operation permits are required by enterprises engaging in the wholesale and/or retail sale of medical devices before commencing the distribution of class II and class III medical devices under the Regulations on the Supervision and Administration of Medical Devices (《醫療器械監督管理條例》). For further information, see "*Regulatory Overview – Operation of Medical Devices – Medical Device Operation Permit*". Out of the 19 pharmacies which do not hold a valid medical device operation permit, (i) seven were established by us and 12 were acquired by us from others, and (ii) 12 have not held a valid medical device operation permit for less than six months, five have not held a valid medical device operation permit for one year to two years, one has not held a valid medical device operation permit for two to three years, and one has lost its medical device operation permit. In 2010, 2011, 2012 and the six months ended 30 June 2013, the amounts of income derived from the operations without the medical device operation permits are approximately RMB0.1 million, RMB2.0 million, RMB2.3 million and RMB1.6 million, respectively. The amounts of profits derived from the operations without the medical device operation permits are approximately RMB0.02 million, RMB0.3 million, RMB0.27 million and RMB0.33 million for the same periods, respectively. The local food and drug administration at or above the county level can order the relevant pharmacies to stop operations and confiscate all illegal products and illegal income. If the illegal income is more than RMB5,000, it can also impose a fine ranging from two to five times of the illegal income. If there is no illegal income or if the illegal income is less than RMB5,000, a fine ranging from RMB5,000 to RMB20,000 can be imposed. In more severe circumstances, these violations may constitute a criminal offence, and the relevant subsidiary can be held criminally responsible. The Company estimates that the maximum amount of potential penalties resulting from the historical non-compliances in relation to the medical device operation permits is approximately RMB600,000.	We have completed the rectifications for 16 of our pharmacies and are in the course of renewing such permits for the other three pharmacies. We have submitted, and the relevant authorities have accepted, our applications for renewal. As advised by our PRC legal advisors, Commerce & Finance Law Offices, there will be no material legal impediments for us to renew the medical device operation permits if we can meet the conditions and requirements under the relevant PRC laws and regulations and undergo the relevant procedures. We currently expect to complete the rectification before the Listing. Based on an interview on 6 November 2013 with a deputy director of Heilongjiang Food and Drug Administrative Bureau (黑龍江省食品藥品監督管理局), which is the competent local authority for the medical device operation permits of the Company's pharmacies in Heilongjiang, it was confirmed by the said deputy director that (a) Heilongjiang Food and Drug Administrative Bureau has not penalised the Group with respect to the required medical device operation permits, and (b) as long as the relevant authorities have accepted the application for renewal of the medical device operation permits submitted by the relevant pharmacies, they will not penalise such pharmacies. Based on (i) the number of pharmacies which do not have the medical device operation permits, (ii) our rectification actions and (iii) the necessary enquires conducted with the relevant authorities as described above, our PRC legal advisors, Commerce & Finance Law Offices, have confirmed that (a) the non-compliances relating to such permits are not material to the Group as a whole, and (b) the risk of being penalised for such historical non-compliances is low in practice once we have renewed such permits.

Matters of non-compliances	Reasons, details and legal consequences of non-compliances	Rectification Actions
(B) Failure to obtain or renew GSP certificates	Due to administrative issues at local authorities, we were not able to obtain or renew the GSP certificates for four of our subsidiaries collectively operating 90 pharmacies. The GSP certificates are required by pharmaceutical retail and wholesale operators under the Administrative Rules on Certification of Good Supply Practice (《藥品經營質量管理規範認證管理辦法》). The new Administrative Rules on Good Supply Practice (《藥品經營質量管理規範》) came into effect on 1 June 2013. The relevant local authorities needed time to discuss and decide how to execute the new rules, which caused the suspension of registration and approval process. For further information, see "*Regulatory Overview – Retail and Distribution of Pharmaceutical Products – Good Supply Practices*". Out of the four subsidiaries which do not hold a valid GSP certificate, (i) all of them were acquired by us from others, and (ii) two are applying for their initial GSP certificates, one has not held a valid GSP certificate for less than one year, and one has not held a valid GSP certificate for one to two years. In 2012 and the six months ended 30 June 2013, the amounts of income derived from the operations without the GSP certificates are approximately RMB45 million and RMB63 million, respectively. The amounts of profits derived from the operations without the GSP certificates are approximately RMB4.3 million and RMB9.3 million for the same periods, respectively.	We are in the course of obtaining or renewing the GSP certificates for the relevant subsidiaries. In particular, (i) the application preparation work in connection with one of our subsidiaries operating 10 pharmacies, Fuhejitai (established in July 2013) is currently being processed, (ii) the application for one of our subsidiaries operating 15 pharmacies, Harbin Jintian Aixin has been accepted pending the verification of the GSP certificate, and (iii) the GSP certificates for two of our subsidiaries collectively operating 65 pharmacies, Heilongjiang Jintian Health Aixin Pharmacy Chain Co., Ltd. (黑龍江省金天健康愛心藥房連鎖有限公司) and Daqing Jintian Aixin Chain Pharmacy Co., Ltd. (大慶金天愛心藥房連鎖有限公司) have expired, however, Jiamusi Food and Drug Administrative Bureau (佳木斯市食品藥品監督管理局) and Daqing Food and Drug Administrative Bureau (大慶市食品藥品監督管理局) have respectively approved the extension to apply for re-certification to January 2014 and June 2014, respectively. However, as advised by our PRC legal advisors, Commerce & Finance Law Offices, we may not be able to obtain the GSP certificates for these subsidiaries until the relevant authorities solve the administrative issues. We will proceed to obtain or renew the GSP certificates for our subsidiaries once the relevant authorities solve the administrative issues and provide clear guidance and instructions. The progress of our rectifications will be disclosed in our interim and annual reports.

Matters of non-compliances	Reasons, details and legal consequences of non-compliances	Rectification Actions
	If the relevant subsidiary cannot get the GSP verification within the specified period regulated by the CFDA, it shall suspend the pharmaceutical distribution business. Failure to do so will result in a warning, and the relevant subsidiary or pharmacy may be ordered to rectify the issue within a specified period and if remedial action is not taken by the prescribed time limit, the relevant subsidiary or pharmacy may be ordered to stop operations and suspend its business, and a fine ranging from RMB5,000 to RMB20,000 per subsidiary can be imposed. In more severe circumstances, the subsidiary or pharmacy may lose its pharmaceutical operation permit. The Company estimates that the maximum amount of potential penalties resulting from the historical non-compliances in relation to the GSP certificates is approximately RMB80,000.	Based on an interview on 29 September 2013 with a director of Heilongjiang Food and Drug Administrative Bureau (黑龍江省食品藥品監督管理局), which is the competent local authority for the GSP certificates of our subsidiaries in Heilongjiang, it was confirmed by such director that (a) details for implementing the new Administrative Rules on Good Supply Practice (《藥品經營質量管理規範》), which became effective on 1 June 2013, are yet to be published by legislative authorities in the PRC and the application and renewal of GSP certificates are suspended for the time being; (b) the Group will not be penalised for failing to apply for or renew the relevant GSP certificates; and (c) the subsidiaries and pharmacies concerned are allowed to operate while the relevant GSP certificates are pending renewal or application. Our PRC legal advisors, Commerce & Finance Law Offices, have advised us that Heilongjiang Food and Drug Administrative Bureau was the competent authority to give such confirmation, and it is unlikely that other higher authorities will challenge such confirmation. Based on (i) the number of pharmacies which do not have the GSP certificates, (ii) our rectification actions and (iii) the necessary inquiries conducted with the relevant authority as described above, our PRC legal advisors, Commerce & Finance Law Offices, have confirmed that (a) the non-compliances relating to such certificates are not material to the Group as a whole, and (b) the risk of being penalised for such historical non-compliances is low in practice once we have obtained or renewed the GSP certificates.

Matters of non-compliances	Reasons, details and legal consequences of non-compliances	Rectification Actions
(C) Failure to obtain or renew health food hygiene permits	Due to administrative issues at local authorities, we were not able to obtain or renew the health food hygiene permits for 138 of our pharmacies, 134 of which are located in Heilongjiang Province. The health food hygiene permits are required for sellers of health food and enterprises engaged in food circulation under the Food Safety Law of the PRC (《中華人民共和國食品安全法》). The Food Safety Law (《食品安全法》) came into effect on 1 June 2009, and after the law came into effect, it was uncertain which local authority was responsible for issuing new permits pursuant to this legislation, which caused the delay in renewing or obtaining such permits for some of our pharmacies. Although it was later clarified that the drug administrative authorities should be the competent authorities to issue the health food hygiene permits, detailed implementation rules are yet to be published by local authorities. If a pharmacy already has a health food hygiene permit, it may apply for an extension of its permit. If a pharmacy does not have a health food hygiene permit, it may not apply for a new permit due to lack of implementation rules in this regard.	We have completed the rectifications for 126 of our pharmacies and are in the course of obtaining or renewing the health food hygiene permits for the other 15 pharmacies (three of which were expired in November 2013). However, as advised by our PRC legal advisors, Commerce & Finance Law Offices, for nine of our pharmacies located in Jiamusi, and other two counties, we may not be able to rectify the non-compliances because detailed implementation rules for application and renewal of health food hygiene permits are yet to be published. In particular, these pharmacies have lost their health food hygiene permits, and therefore cannot apply for extension for such permits. We will proceed to obtain or renew the health food hygiene permits for these pharmacies once the relevant authorities solve the administrative issues and provide clear guidance and instructions. The progress of our rectifications will be disclosed in our interim and annual reports. For the other six pharmacies, our PRC legal advisors, Commerce & Finance Law Offices, have advised us that there will be no material legal impediments for us to obtain or renew the health food hygiene permits. We currently expect to complete the rectification before Listing.

Matters of non-compliances	Reasons, details and legal consequences of non-compliances	Rectification Actions
		Based on an interview on 10 October 2013 with a director of Jiamusi Food and Drug Administrative Bureau (佳木斯食品藥品監督管理局), which is the competent local authority for the health food hygiene permits of the Company's subsidiaries in Jiamusi, it was confirmed by such director that (a) after the Food Safety Law came into effect on 1 June 2009 and up to 2012, the application and renewal of health food hygiene permits was suspended in Jiamusi as it was uncertain which authority was responsible for issuing such permits pursuant to this legislation and (b) although it was later clarified that the drug administrative authorities should be the competent authorities in issuing such permits, detailed implementation rules for the application and renewal of such permits are yet to be published by Heilongjiang Food Drug Administrative Bureau (黑龍江省食品藥品監督管理局), the Group will not be penalised for failing to apply for or renew the relevant health food hygiene permits and the pharmacies concerned are allowed to operate while the relevant health food hygiene permits are pending renewal or application. Our PRC legal advisors, Commerce & Finance Law Offices, have advised us that Jiamusi Food and Drug Administrative Bureau was the competent authority to give such confirmation and it is unlikely that other higher authorities will challenge such confirmation.

Matters of non-compliances	Reasons, details and legal consequences of non-compliances	Rectification Actions
		Based on an interview on 6 November 2013 with a director of Heilongjiang Food and Drug Administrative Bureau (黑龍江省食品藥品監督管理局), which is the competent local authority for the health food hygiene permits of the Company's pharmacies in Heilongjiang, it was confirmed by such director that (a) there are currently administrative issues relating to the implementation of food safety laws and detailed implementation rules for the application and renewal of the health food hygiene permits are yet to be published, (b) the relevant pharmacies will be allowed to continue their operations while the health food hygiene permits are pending renewal or application, and (c) Heilongjiang Food and Drug Administrative Bureau will not penalise the relevant pharmacies solely based on the absence of the required health food hygiene permits.

Matters of non-compliances	Reasons, details and legal consequences of non-compliances	Rectification Actions
	We are still waiting for the relevant local authorities to provide clear guidance in relation to the issuance of such permits. For further information, see "*Regulatory Overview – Distribution of Health Food – Health Food Hygiene Permit*". Out of the 138 pharmacies which do not hold a valid health food hygiene permit, (i) 50 were established by us and 88 were acquired by us from others, and (ii) 36 have not held a valid health food hygiene permit for less than one year, 48 have not held a valid health food hygiene permit for one to two years, 13 have not held a valid health food hygiene permit for two to three years, 20 have not held a valid health food hygiene permit for more than three years, and 21 have lost their health food hygiene permits. In 2010, 2011, 2012 and the six months ended 30 June 2013, the amounts of income derived from the operations without the health food hygiene permits are approximately RMB4.9 million, RMB17.4 million, RMB22.4 million and RMB7.5 million, respectively. The amounts of profits derived from the operations without the health food hygiene permits are approximately RMB1.9 million, RMB6.4 million, RMB6.2 million and RMB2.3 million for the same periods, respectively. The relevant authorities can confiscate all illegal income, illegal products, tools, equipment and raw materials utilised in connection with such operations. If the value of the illegal food items is less than RMB10,000, a fine ranging from RMB2,000 to RMB50,000 can be imposed. If the value of the illegal food items is more than RMB10,000, a fine of five times to ten times of such value can be imposed. The Company estimates that the maximum amount of potential penalties resulting from the historical non-compliances in relation to the health food hygiene permits is approximately RMB6,300,000.	Based on (i) the number of pharmacies which do not have the health food hygiene permits, (ii) our rectification actions and (iii) the necessary enquiries conducted with the relevant authorities as described above, our PRC legal advisors, Commerce & Finance Law Offices, have confirmed that (a) the non-compliances relating to such permits are not material to the Group as a whole, and (b) the risk of being penalised for such historical non-compliances is low in practice once we have obtained or renewed such permits.

Matters of non-compliances	Reasons, details and legal consequences of non-compliances	Rectification Actions
(D) Failure to make housing fund contributions for our employees	Due to administrative oversight, all of our PRC subsidiaries did not make housing fund contributions for their employees. Out of these subsidiaries, (i) seven were established by us or the Controlling Shareholders and 11 were acquired by us from others; and (ii) four have not made housing fund contributions for less than one year, 10 have not made housing fund contributions for one to three years, two have not made housing fund contributions for three to five years and two have not made housing fund contributions for more than five years. An employer that fails to pay its housing fund contributions in a timely manner may be subject to a penalty of up to RMB50,000 and court enforcement order in certain situations. The Company estimates that the maximum amount of potential penalties resulting from the historical non-compliances in relation to housing fund contributions is approximately RMB800,000.	As at 30 June 2013, we have set aside RMB10.1 million in total to rectify our non-compliances in relation to housing fund contributions. While 13 subsidiaries of the Group have opened housing fund accounts and 11 subsidiaries have started to make the required housing fund contribution, all the other subsidiaries of the Group will start to make such contributions in November 2013. Going forward, we will pay the required housing fund contributions for all of our employees and monitor our compliance on an on-going basis. Based on the RMB10.1 million set aside to rectify such non-compliances and other rectification actions taken by the Group as described above, our PRC legal advisors, Commerce & Finance Law Offices, have confirmed that (a) the non-compliances relating to such contributions are not material to the Group as a whole, and (b) the risk of being penalised for such historical non-compliances is low in practice once we have rectified such non-compliances pursuant to relevant PRC laws and regulations.

Matters of non-compliances	Reasons, details and legal consequences of non-compliances	Rectification Actions
(E) Failure to make part of the social insurance contributions for our employees	Due to administrative oversight, five of our PRC subsidiaries did not make part of the social insurance contributions for their employees. Out of these subsidiaries, (i) one was established by the Controlling Shareholders and four were acquired by us from others; and (ii) four have not made social insurance contributions for less than one year and one has not made social insurance contributions for two to three years. An employer that fails to pay its social insurance contributions in a timely manner may be subject to a fine equal to 0.05% per day of the amount due, and in certain situations, a fine equal to three times of the amount due.	As at 30 June 2013, we have set aside RMB10.6 million in total to rectify our non-compliances in relation to social insurance contributions. While two subsidiaries of the Group have rectified the non-compliances and started to make the required social insurance contribution, the other three subsidiaries will start to make such contributions in November 2013. Going forward, we will pay the required social insurance contribution for all of our employees and monitor our compliance on an on-going basis. Based on the RMB10.6 million set aside to rectify such non-compliances and other rectification actions taken by the Group as described above, our PRC legal advisors, Commerce & Finance Law Offices, have confirmed that (a) the non-compliances relating to such contributions are not material to the Group as a whole, and (b) the risk of being penalised for such historical non-compliances is low in practice once we have rectified such non-compliances pursuant to relevant PRC laws and regulations.

Our PRC legal advisors, Commerce & Finance Law Offices, are of the view that these non-compliance incidents, whether individually or collectively, are not material to the Group as a whole, and all the PRC governmental authorities referred to in the above table are the competent authorities for the respective matters mentioned in such table. Our PRC legal advisors, Commerce & Finance Law Offices, have also confirmed that except for the administrative issues at local authorities in relation to the GSP certificates and health food hygiene permits, they are not aware of any material legal impediment in obtaining or renewing the outstanding licences and permits.

Our Directors are of the view that these non-compliance incidents, whether individually or collectively, will not have a material operational or financial impact on us. Therefore, it will be in the interests of the Group and the Shareholders not to cease the operations of the relevant subsidiaries or pharmacies. Having considered the latest status of the application, renewal and the nature of the licences and permits we had failed to obtain or which had expired, as at the Latest Practicable Date, there were no outstanding licences or permits which would have a material adverse effect on the operations of the Group.

The Company undertakes that it will rectify all non-compliances in a timely manner once the relevant authorities resolve the administrative issues and provide clear guidance in relation to application or renewal of the relevant licences and permits, and will update the progress of the rectification of the non-compliance incidents in the Company's interim and annual reports after the Listing.

Whilst the non-compliances in relation to the GSP certificates and health food hygiene permits were due to administrative issues at the local authorities, the non-compliances in relation to medical device operation permits and housing fund and social insurance contributions were due to our administrative oversight. Although the Directors are responsible for the overall operations of the Group, such non-compliances were not due to lack of experience, integrity, skill, care or diligence of the Directors. Our Directors have contributed sufficient amount of time on the overall business operations and growth of our Group, have been dedicated to the daily management and the long term objects to advance the Shareholders' interests. However, given the large number of the Group's subsidiaries and pharmacies, it is impractical for the Directors to be heavily involved in the daily operations of each of such subsidiaries and pharmacies. The Directors have been relying on the managers of the local subsidiaries and pharmacies to carry out the daily operations of the Group and implement the relevant internal control measures.

In preparation for the Listing, we engaged an independent business consulting and internal audit firm (the "**Internal Control Consultant**") to conduct an evaluation of our internal control system. We have consulted with our Internal Control Consultant to identify the factors relevant to enhancing our internal control system and the steps to be taken and the Internal Control Consultant made a number of recommendations.

In relation to the licences and permits, the Internal Control Consultant recommended that: (i) the Group should adopt a set of internal control policies regarding the application and renewal of licences and permits, (ii) an internal control coordinator should be appointed in each of the Group's operating subsidiaries, who will be responsible for the application and renewal of the licences and permits and monitor their status and (iii) the status of the relevant licences and permits should be periodically reported to the headquarters of the Group.

In relation to the housing fund and social insurance contributions, the Internal Control Consultant recommended that (i) the human resource department in each of the Group's operating subsidiaries shall monitor the status of housing fund and social insurance contributions for the employees and (ii) the senior management of the operating subsidiaries shall periodically review the Group's compliance with laws and regulations in relation to housing fund and social insurance contributions.

The Group started to implement the recommendations in relation to the licences and permits in August 2013 and the recommendations in relation to the housing fund and social insurance contributions in September 2013. As of the Latest Practicable Date, such recommendations had been fully implemented.

Ms. Chen will be responsible for implementing the internal control measures of the Group. She will report to Mr. Jin. Please see "*Directors and Senior Management*" for the relevant experience and qualifications of Ms. Chen. Ms. Chen has been in charge of the internal control matters of the Group since 2008. She is familiar with the relevant conditions and requirements and has extensive experience of communicating with relevant authorities in relation to the application for and renewal of various licences and permits of the Group.

In response to the Internal Control Consultant's recommendations in relation to licences and permits, the Company has adopted internal control measures to review and monitor the application and renewal of its licences and permits. Under such measures, an internal control coordinator, who has previous experience of applying for and renewing the relevant licences and permits, has been appointed in each of our operating subsidiaries. They are responsible for the application and renewal of our licences and permits. Each internal control coordinator will prepare and maintain a matrix, which sets out, among other things, all the required licences and permits for our subsidiaries, the status of obtaining or renewal of such licences and permits, relevant expiry dates and potential impact for failing to obtain or renew such licences and permits. The matrix will be updated monthly and submitted to the headquarters of the Group.

In response to the Internal Control Consultant's recommendations in relation to the payment of housing fund and social insurance contributions, the Company has adopted internal control measures to review and monitor payment of housing fund and social insurance contributions. Under such measures, the human resource department in each of our operating subsidiaries will prepare a matrix, which sets out, among other things, a list of employees, the required types of contributions, the amounts due and time for such payments. The general managers of our operating subsidiaries will periodically review our compliance with laws and regulations in relation to housing fund and social insurance contributions.

We have also recently adopted a series of internal control measures to enhance our internal control in respect of procurement, quality control, inventory management and sales activities. In particular:

(i) we have established a centralised procurement platform with the power of procurement vested in a procurement department in the headquarters of the Group. This centralised procurement model not only provides benefits associated with bulk purchases and scale operations but also a higher degree of control over the product qualities. The central procurement department is in charge of the procurement of the full spectrum of our products, including, among other products, our Licensed Products and the products with exclusive distribution rights. Furthermore, we have put relevant personnel in place to be responsible for each aspect of supplier evaluation, contract negotiation, purchase order review, quality control inspection and inventory management;

(ii) we have established several business review teams which are led by our general managers. These teams aim to improve the operations and performance of each of our pharmacies by periodically conducting a comprehensive business review in respect of certain important aspects, including but not limited to, quality control inspection, inventory management, customer services and sales activities;

(iii) we have upgraded the information technology system and inventory management software of the central procurement department so that it will be able to implement real-time monitoring, inspection and analysis of our inventory and product mix throughout the entire procurement process. Monthly reports are prepared and brought to the attention of the Directors if any major issues on quality control are identified by the central procurement department;

(iv) we have organised some training programmes focusing on quality control issues for our employees in order to enhance their awareness and sense of responsibility on quality control. We have also developed a set of internal control policies setting out the policies and procedures for procurement management, supplier evaluation and inventory management. Under these policies, we will accept pharmaceutical products only if (i) the suppliers can provide us with the product quality verification reports prepared by the relevant manufacturers and (ii) our internal quality control department is satisfied with the product quality after appropriate inspection. We will conduct new supplier evaluation when choosing new suppliers based on their backgrounds, qualification status and operating histories. We will periodically review the performance of our existing suppliers based on the quality and price of the pharmaceutical products provided. If any supplier is found to have provided us with pharmaceutical products involving quality issues, we will immediately cease doing business with such supplier. We have also enhanced our inventory management to maintain the quality of the products stored in our warehouses. All of our employees are required to attend such training programs and familiarise themselves with such internal control policies; and

(v) we will educate the relevant personnel who violates our internal control measures on quality control and a notice regarding such incidents will be circulated internally as an alert to other employees. We have also developed a store/regional manager responsibility system. Under this system, if a pharmacy is found to be liable for any quality control incidents, e.g., selling counterfeit products, the relevant store/regional managers in charge of the pharmacy must (a) fully investigate the incident and prepare a report for the consideration of the Directors, and (b) review the deficiencies in his management and supervision on quality control and propose as well as implement effective preventive measures to avoid occurrence of similar incidents in the future.

With a view to testing the adequacy and effectiveness of the enhanced internal control measures which have been implemented only recently, the Internal Control Consultant has conducted sample testing of the Group's internal control measures in relation to quality control, licences and permits and housing fund and social insurance contributions. Based on such review and other due diligence work performed to test our effectiveness in implementing these measures, the Internal Control Consultant has confirmed that (i) all the relevant measures have been carried out effectively and no material deficiency was identified, and (ii) the measures set out above are adequate and effective in enhancing our internal control and quality control. After considering the view of the Internal Control Consultant and based on the relevant due diligence work conducted, the Sole Sponsor is of the view that the above internal control and quality control measures are adequate and effective in enhancing our internal control and quality control.

Based on the above, the Directors consider that the above internal control measures should be sufficient for the purpose of ensuring ongoing material compliance with the relevant laws and regulations concerning product quality, the validity of the licences and permits and housing fund and social insurance contributions.