

CHINA MEDICAL SCIENCE LIMITED

中華藥業有限公司*

(Incorporated in the Cayman Islands with limited liability)

THIRD QUARTERLY REPORT

2002

** For identification purposes only*

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This report, for which the directors of CHINA MEDICAL SCIENCE LIMITED collectively and individually accept full responsibility, includes particulars given in compliance with Rules Governing the Listing of Securities on the GEM for the purpose of giving information with regard to CHINA MEDICAL SCIENCE LIMITED. The directors of CHINA MEDICAL SCIENCE LIMITED, having made all reasonable enquires, confirm that, to the best of their knowledge and belief: (i) the information contained in this report is accurate and complete in all material respects and not misleading; (ii) there are no other matters the omission of which would make any statement in this report misleading; and (iii) all opinions expressed in this report have been arrived at after due and careful consideration and are founded on bases and assumptions that are fair and reasonable.

HIGHLIGHTS

- Turnover of the Group for the nine months ended 30 April 2002, amounted to approximately HK\$132,485,000, representing an increase of approximately 11.6% as compared with the corresponding period in 2001.
- Net profit attributable to shareholders for the nine months ended 30 April 2002 amounted to approximately HK\$14,188,000, compared with a profit of HK\$17,611,000 recorded by the Group in the corresponding period in 2001.
- Basic earnings per share amounted to approximately 2.84 cents for the nine months ended 30 April 2002.
- The Directors do not recommend the payment of an interim dividend for the nine months ended 30 April 2002.

RESULTS

The Board of Directors (the “Board”) of China Medical Science Limited (the “Company”) is pleased to announce that the unaudited consolidated results of the Company and its subsidiaries (collectively, the “Group”) for the three months and nine months ended 30 April 2002 together with unaudited comparative figures for the corresponding period in 2001, are as follows:

Consolidated Profit and Loss Account - Unaudited

	<i>Note</i>	For the three months ended 30 April		For the nine months ended 30 April	
		2002 <i>HK\$'000</i>	2001 <i>HK\$'000</i>	2002 <i>HK\$'000</i>	2001 <i>HK\$'000</i>
Turnover	2	42,520	41,266	132,485	118,755
Cost of sales		<u>(28,462)</u>	<u>(26,187)</u>	<u>(89,291)</u>	<u>(75,859)</u>
Gross profit		14,058	15,079	43,194	42,896
Other revenue		732	414	1,670	720
Selling and distribution expenses		(2,777)	(2,985)	(7,630)	(9,110)
General and administration expenses		(2,652)	(2,990)	(10,378)	(7,881)
Other operating expenses		<u>(1,562)</u>	<u>(960)</u>	<u>(3,605)</u>	<u>(2,890)</u>
PROFIT FROM OPERATING ACTIVITIES		7,799	8,558	23,251	23,735
Finance costs		<u>(2,731)</u>	<u>(1,742)</u>	<u>(7,545)</u>	<u>(4,327)</u>
PROFIT BEFORE TAXATION		5,068	6,816	15,706	19,408
Taxation	3	<u>—</u>	<u>—</u>	<u>—</u>	<u>—</u>
PROFIT BEFORE MINORITY INTEREST		5,068	6,816	15,706	19,408
Minority interest		<u>(500)</u>	<u>(662)</u>	<u>(1,518)</u>	<u>(1,797)</u>
NET PROFIT ATTRIBUTABLE TO SHAREHOLDERS		<u>4,568</u>	<u>6,154</u>	<u>14,188</u>	<u>17,611</u>
EARNINGS PER SHARE	4				
- Basic		<u>0.91 cents</u>	<u>1.50 cents</u>	<u>2.84 cents</u>	<u>4.30 cents</u>
- Diluted		<u>0.87 cents</u>	<u>1.50 cents</u>	<u>2.70 cents</u>	<u>4.26 cents</u>

1. Group reorganization and basis of presentation

The Company was incorporated as an exempted company with limited liability in the Cayman Islands on 22 September 2000 under the Companies Law (2000 Revision) of the Cayman Islands. Pursuant to a group reorganisation completed on 23 March 2001 (the “Reorganisation”) to rationalize the Group’s structure in preparation for the listing of the shares on GEM, the Company became the holding company of the companies now comprising the Group. The Company’s shares have been listed on the GEM since 10 April 2001.

The results of the Group have been prepared using the merger basis of accounting. On this basis, the Company has been treated as the holding company of its subsidiaries acquired through the Reorganisation for both the financial periods presented, rather than from the date of their acquisition pursuant to the Reorganisation on 23 March 2001.

The principal accounting policies adopted in preparing the unaudited consolidated results conform with the Statements of Standard Accounting Practice and Interpretations issued by the Hong Kong Society of Accountants, the disclosure requirements of Hong Kong Companies Ordinance and the Rules Governing the Listing of Securities on the Growth Enterprise Market of The Stock Exchange of Hong Kong Limited (“GEM Listing Rules”).

Several new accounting standards issued by the Hong Kong Society of Accountants are effective for this financial period. These accounting standards except in relation to SSAP 30 “Business Combination” have no material impact on the reported financial position or results of the China Medical Group.

In accordance with the SSAP 30, the negative goodwill is required to present as a deduction from the assets in the balance sheet and to be recognized as income in the profit and loss account on a systematic basis over the remaining weighted average useful life of the identifiable acquired depreciable assets; the goodwill is amortised to the profit and loss account over its estimated useful life.

In prior years, goodwill (negative goodwill) arising on acquisition was eliminated against reserves in the year of acquisition. The Group has adopted the transitional provision of SSAP 30 that permits goodwill (negative goodwill) on acquisitions occurred prior to 1 January 2001, to recognize as a separately identified item on the consolidated balance sheet and to be recognized as expense or income in the profit and loss account on a systematic basis.

2. Turnover

The Group's turnover represents the net invoiced value of goods sold, net of value added tax, and after allowances for returns and trade discounts.

	For the three months ended 30 April		For the nine months ended 30 April	
	2002	2001	2002	2001
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Sale of human drugs				
— infusion medicine	23,464	18,473	70,978	47,879
Sale of veterinary drugs	7,798	9,884	22,199	26,646
Sale of packaging materials for infusion medicine	11,258	12,909	39,308	44,230
	<u>42,520</u>	<u>41,266</u>	<u>132,485</u>	<u>118,755</u>

3. Taxation

No provision for Hong Kong profits tax has been made, as the Group had no assessable profits arising in Hong Kong during the period ended 30 April 2002. (2001: Nil)

No provision for PRC corporate income tax has been made for the nine months ended 30 April 2002 as all the subsidiaries of the Group in the PRC are exempted from PRC corporate income tax for the first two profitable years of operation and are entitled to a 50% relief from corporate income tax for the following three years.

The Group did not have any significant unprovided deferred tax liabilities in respect of the period ended 30 April 2002. (2001: Nil)

4. Basic earnings per share

The calculation of the basic earnings per share for the three months and nine months ended 30 April 2002 is based on the unaudited net profit attributable to shareholders of approximately HK\$4,568,000 and approximately HK\$14,188,000 respectively (three months and nine months ended 30 April 2001: net profit of approximately HK\$6,154,000 and approximately HK\$17,611,000 respectively) and the weighted average number of 500,000,000 ordinary shares for the three months and nine months ended 30 April 2002 (three months and nine months ended 30 April 2001: weighted number of 410,000,000 ordinary shares in issue).

The calculation of diluted earnings per share for the three months and nine months ended 30 April 2002 is based on the Group's unaudited net profit attributable to shareholders of approximately HK\$4,763,000 and approximately HK\$14,788,000 respectively (three months and nine months ended 30 April 2001: net profit of approximately HK\$6,199,000 and approximately HK\$17,656,000 respectively), after adjustment of interest saved upon deemed conversion of all convertible notes (the "Convertible Note") upon listing, and the weighted average number of 500,000,000 ordinary shares (three months and nine months ended 30 April 2001: weighted number of 410,000,000 ordinary shares in issue) outstanding plus the respective weighted average number of 48,619,564 ordinary shares (2001: 4,357,077 ordinary shares) deemed to be issued as if the Convertible Note had been converted upon the listing.

5. Reserves

Movements in the reserves of the Group during the nine months ended 30 April 2002 are summarised as follows:

	Share premium <i>HK\$'000</i>	Capital reserve <i>HK\$'000</i>	Exchange fluctuation reserve <i>HK\$'000</i>	Retained profit <i>HK\$'000</i>	Total <i>HK\$'000</i>
At 31 July 2001					
As previously reported	17,992	27,728	25	29,403	75,148
Prior year adjustments (Note 1)	—	(625)	—	326	(299)
As restated	17,992	27,103	25	29,729	74,849
Profit for the period	—	—	—	14,188	14,188
At 30 April 2002	<u>17,992</u>	<u>27,103</u>	<u>25</u>	<u>43,917</u>	<u>89,037</u>

6. Comparative figures

Certain comparative figures have been reclassified on the face of the consolidated profit and loss accounts to conform to current period's presentation.

INTERIM DIVIDEND

The Directors do not recommend the payment of an interim dividend for the nine months ended 30 April 2002. (2001: Nil)

BUSINESS REVIEW

ANALYSIS OF RESULTS

For the three months and nine months ended 30 April 2002, turnover generated from sale of medical caps for infusion medicine, veterinary drugs and human drugs amounted to approximately HK\$42,520,000 and HK\$132,485,000 respectively, representing an increase of approximately 3% and 11.6% respectively as compared with the turnover of the corresponding period in 2001. However, with a series of reforms implemented by the State in the pricing and tendering system for pharmaceutical products, the profit margin of our infusion medicines was put under considerable pressure. In addition, the Group also experienced fierce competitions in the PRC pharmaceutical market. As a result, the Group's net profit decreased by approximately 19.4% when compared with the corresponding period ended 30 April 2001.

Chengdu Mt. Green Pharmaceutical Co., Ltd. ("Chengdu Mt. Green")

- 1) The sale of infusion medicine by Chengdu Mt. Green for the 3-month ended 30 April 2002 amounted to approximately HK\$23,464,000, representing approximately 27% higher than that of the corresponding period in the preceding year.
- 2) During the period under review, the State implemented reforms on the pricing system for at least five hundred pharmaceutical products, resulting in a price reduction for these products. Meanwhile, the newly implemented tendering system also caused a drop in the profit margin. In the light of these changes in the PRC pharmaceutical market, the company implemented various management measures to enhance operational efficiency, reduce production cost and achieve economies of scale.
- 3) Through the implementation of new commission-based remuneration measure for the sales-force, the company will place more emphasis on market expansion and explore potential provincial and urban areas so as to further increase the penetration of products in the domestic market and enhance the products image in the industry. In addition, the company will further strengthen the credit control of accounts receivable and speed up the collection process.

Sichuan Future Industrial Co., Ltd. (“Sichuan Future”)

- 1) The sale of packaging materials for infusion medicine for the 3-month period under review amounted to approximately HK\$11,258,000, representing a decrease of approximately 12.8% from the sales recorded in the corresponding period in the preceding year.
- 2) With the full recognition and positive appraisal from the SDA and Sichuan Drugs Administration in respect of the national pilot GMP standard for the packaging materials in the second quarter, Sichuan Future, during the 3-month period under review, further achieved cost savings and optimised overall production process. This was achieved through the enhancement of production management and the adoption of a flexible and diverse market-oriented operational model. We achieved more than 15% growth in production capacity as compared with the second quarter.
- 3) The new multi-coloured transparent aluminium-plastic caps with high molecule material coating have been well received by the market since they were launched. This will provide an additional source of income to the company in the future.

Chengdu Viking Yuan Heng Pharmaceutical Co., Ltd. (“Chengdu Yuan Heng”)

- 1) The sale of veterinary drugs for the 3-month period under review amounted to approximately HK\$7,798,000, representing an approximate 21.1% decrease from the sales recorded in the corresponding period in the preceding year, mainly as a result of the traditional Chinese New Year holiday.
- 2) Amongst three newly built production workshops - the powdered medicine workshop, the orally administrated liquid medicine workshop and the Chinese medicine extraction workshop, the Chinese medicine extraction workshop has been in operation since 2001. Currently the air-purifying works and overall infrastructures of the powdered medicine workshop and the orally administrated liquid medicine workshop have just been completed. The latter two workshops are expected to operate in the next quarter.
- 3) Through the expansion of the sale force, the sale in other regions of PRC has improved considerably. Currently the sales in other regions are about 70% of the total sales, and this trend will go further.

Research and Development

Currently Chengdu Mt. Green has a variety of infusion medicines in the research and development pipeline. During the period under review, the company was making good progress in its negotiation with Chengdu Chinese Medicine Research Institute and the Chief Hospital of the Military Region for the development and transplantation of new Chinese medicine. In addition, more overseas-patented medicines will be introduced under the joint-cooperation with ABC Lifescience Inc. This will further expedite Chengdu Mt. Green's development of new therapeutic infusion medicines and its establishment of a systematic sales network in the whole country. Capitalizing the new medical technologies, the company paves its way to modernize the traditional mode of medicines and to expand into natural-medicine products.

For veterinary drugs, Chengdu Yuan Heng obtained pharmaceutical registration for Compound Sulfavhlorpyridazine Sodium Powder and Robenidine Hydrochloride Premix during the 3-month period under review.

OUTLOOK

China's accession into the World Trade Organization will broaden her access to advanced research and development and production technologies. This will also bring about unlimited business opportunities for the Group. The Group will actively explore and identify suitable investment opportunities in focused areas in the PRC. With further progress in the research and development of new products and the continued expansion and consolidation of the Group's operations, sales and distribution network, the Directors are confident that the Group will outpace growth in the PRC pharmaceutical market, and generate profitable returns for its shareholders.

COMPETING INTEREST

None of the directors, the management shareholders, significant shareholders and substantial shareholders (as defined in the GEM Listing Rules) of the Company had any interest in any business, which competes or may compete with the business of the Group.

DIRECTORS' INTERESTS IN THE SHARES OF THE COMPANY

As at 30 April 2002, the interests of the directors and their associates in the share capital of the Company and its associated corporations, as recorded in the register maintained by the Company pursuant to Section 29 of the Securities (Disclosure of Interests) Ordinance (“SDI Ordinance”) or as otherwise notified to the Company pursuant to the minimum standards of dealings by the directors as referred to Rule 5.4 of the GEM Listing Rules were as follows:

Name of Director	Nature of Interest	Number of shares in the Company
Mr. Wong Sai Chung (<i>Note a</i>)	Corporate interest	400,000,000

Note:

- (a) The shareholding interest attributable to Mr. Wong Sai Chung, an executive Director, in the Company is held through Concord Pharmaceutical Technology (Holdings) Limited and Concord Business Management Limited. Concord Pharmaceutical Technology (Holdings) Limited and Concord Business Management Limited are investment holding companies and wholly-owned by Mr. Wong Sai Chung.

Saves as disclosed above, none of the directors or their associates had any personal, family, corporate or other interests in the equity or debt securities of the Company or any of its associated corporations as defined in the SDI Ordinance.

DIRECTORS' RIGHTS TO ACQUIRE SHARES

Pursuant to the terms of the Company's Pre-IPO Share Option Scheme (the “Pre-IPO Plan”) adopted by the Company on 23 March 2001, the Company has granted options to the following Directors to subscribe for shares in the Company at any time from 10 October 2001 up to and including 9 April 2011 at an exercise price of HK\$ 0.55 per Share. Summary details of these options which remain outstanding as at 30 April 2002 are as follows:

Name of Director	Number of underlying shares
Mr. Wong Sai Wa	3,200,000
Mr. Kwan Kai Cheong	3,000,000

The exercise period of the Pre-IPO Plan is set out under the paragraph headed “Share Option Schemes” below. Details of the Pre-IPO Plan are set out in the Prospectus.

Pursuant to the Convertible Note issued by the Company on 23 March 2001, the following director has personal interests in the Convertible Note convertible into shares of the Company:

Name of Director	Outstanding principal	Number of underlying shares
Mr. Wong Sai Chung (<i>Note</i>)	HK\$26,740,760.00	48,619,564

Note: The shareholding interest attributable to Mr. Wong Sai Chung in the Company is held through Concord Pharmaceutical Technology (Holdings) Limited and Concord Business Management Limited, each of Concord Pharmaceutical Technology (Holdings) Limited and Concord Business Management Limited is an investment holding company wholly-owned by Mr. Wong Sai Chung who is an executive Director of the Company.

The principal terms of the Convertible Note are set out in the Prospectus.

Save as disclosed above, at no time during the period was the Company or any of its subsidiaries a party to any arrangements to enable the Company's directors, their respective spouse or children under 18 years of age to acquire benefits by means of acquisition of shares in or debentures of the Company or any other body corporate.

SHARE OPTION SCHEMES

On 23 March 2001, the Company conditionally adopted the Pre-IPO Plan and the Share Option Scheme, the principal terms of which are set out in the Prospectus.

Pursuant to the Pre-IPO Plan, five employees of the Group (including two executive Directors) were conditionally granted options on 23 March 2001 to subscribe for an aggregate of 7,400,000 shares, which upon exercise in full will result in the issue of 7,400,000 additional ordinary shares of HK\$0.05 each for the aggregate proceeds of HK\$4,070,000 before the related shares issue expense. All of these options have a duration of 10 years from the date of grant of the options, each is exercisable in accordance with their terms of issue after 6 months from the date of listing of the shares on GEM, but each shall lapse if the relevant grantee ceases to be employed by the relevant companies. The option of 400,000 shares granted to Ms. Yip Yuk Lin, the former certified accountant, was cancelled on 17 August 2001 due to her resignation from the Group. Therefore, as at 30 April 2002, the number of share options granted to the employees was 7,000,000 shares. The aggregate amount of HK\$3,850,000 will be generated if all share options are fully exercised. As at 30 April 2002, none of the Directors or employees of the Company had exercised any share options and no allotment or issue of shares was made pursuant to the Pre-IPO Plan.

On 23 March 2001, the Company adopted a Share Option Scheme (the “Share Option Scheme”) under which the Board of the Company may at their discretion, grant options to full time employees of the Group, including any executive directors of the Company and any of its subsidiaries, to subscribe for shares in the Company in accordance with the provisions in the Share Option Scheme. The Share Option Scheme became effective upon the listing of the Company on the GEM on 23 March 2001 for a period of ten years. Further details of the Share Option Scheme are set out in the Prospectus. No options were granted under the Share Option Scheme during the period.

Save as disclosed herein, no rights to acquire benefits by means of the acquisition of shares in or debentures of the Company were granted to any director, chief executive and substantial shareholder of the Company or their respective associates.

SUBSTANTIAL SHAREHOLDERS

As at 30 April 2002, save for interests of Directors disclosed above, the register of substantial shareholders maintained by the Company under Section 16(1) of the SDI Ordinance showed that the following interests, being 10% or more in the Company’s issued share capital:

Name of shareholder	Number of shares held	% of shareholding
Concord Pharmaceutical Technology (Holdings) Limited (<i>Note</i>)	400,000,000	80
Concord Business Management Limited (<i>Note</i>)	400,000,000	80
Mr. Wong Sai Chung (<i>Note</i>)	400,000,000	80

Note: Concord Pharmaceutical Technology (Holdings) Limited is a wholly-owned subsidiary of Concord Business Management Limited, the entire issued share capital of which is owned by Mr. Wong Sai Chung. Accordingly, each of Concord Business Management Limited and Mr. Wong Sai Chung is deemed to have an interest in the 400,000,000 shares of the Company held by Concord Pharmaceutical Technology (Holdings) Limited.

SPONSOR’S INTEREST

Pursuant to the Sponsor’s agreement dated 3 May 2001 entered into between the Company and Core Pacific - Yamaichi Capital Limited (the “Sponsor”), the Sponsor has received and will receive a fee for acting as the Company’s retained sponsor for the period from 3 May 2001 to 31 July 2003.

Saved as disclosed above, as at 30 April 2002, the Sponsor, its directors, employees or associates, did not have any interest in the securities of the Company and any members of the Group, or any right to subscribe for or to nominate persons to subscribe for the securities of the Company or any members of the Group.

AUDIT COMMITTEE

The Company set up an audit committee on 23 March 2001 with written terms of reference in compliance with the requirements as set out in rules 5.23, 5.24 and 5.25 of the GEM Listing Rules. The committee comprises two independent non-executive directors of the Company. The primary duties of the audit committee are to review and provide supervision over the financial reporting process and internal control of the Group.

COMPLIANCE WITH BOARD PRACTICE AND PROCEDURES

For the 9-month period under review, the Company has complied with the board practices and procedures as set out in Rules 5.28 to 5.39 of the GEM Listing Rules.

PURCHASE, SALE OR REDEMPTION

During the nine months ended 30 April 2002, neither the Company nor any of its subsidiaries had purchased, sold or redeemed any of the Company's listed securities.

By Order of the Board
Wong Sai Chung
Chairman

Hong Kong, 13 June, 2002