



# **MEDICAL CHINA LIMITED**

*(Incorporated in Bermuda with limited liability)*

## **Annual Report 2002**

## **CHARACTERISTICS OF THE GROWTH ENTERPRISE MARKET (GEM) OF THE STOCK EXCHANGE OF HONG KONG LIMITED (THE STOCK EXCHANGE)**

GEM has been established as a market designed to accommodate companies to which a high investment risk may be attached. In particular, companies may list on GEM with neither a track record of profitability nor any obligation to forecast future profitability. Furthermore, there may be risks arising out of the emerging nature of companies listed on GEM and the business sectors or countries in which the companies operate. Prospective investors should be aware of the potential risks of investing in such companies and should make the decision to invest only after due and careful consideration. The greater risk profile and other characteristics of GEM mean that it is a market more suited to professional and other sophisticated investors.

Given the emerging nature of companies listed on GEM, there is a risk that securities traded on GEM may be more susceptible to high market volatility than securities traded on the Main Board and no assurance is given that there will be a liquid market in the securities traded on GEM.

The principal means of information dissemination on GEM is publication on the internet website operated by the Exchange. Listed companies are not generally required to issue paid announcements in gazetted newspapers. Accordingly, prospective investors should note that they need to have access to the GEM website in order to obtain up-to-date information on GEM-listed issuers.

# Contents

Corporate Information	3
Chairman's Statement	4
Management Discussion and Analysis	6
Directors and Senior Executives	17
Report of the Directors	19
Auditors' Report	26
Consolidated Income Statement	27
Consolidated Balance Sheet	28
Balance Sheet	30
Consolidated Statement of	
Changes in Equity	31
Consolidated Cash Flow Statement	32
Notes to the Financial Statements	34
Three Years' Summary	68

# Corporate Information

## BOARD OF DIRECTORS

### Executive directors

LI Nga Kuk, James (*Chairman*)

LI Wo Hing (*General Manager*)

NG Kwai Sang

CHAN Shut Li, William

CHAN Siu Sun

LI Tai To, Titus

### Non-executive directors

CHEN Minshan

### Independent non-executive directors

GUO Guoqing

FAN Wan Tat

HAN K. Huang

## COMPLIANCE OFFICER

LI Wo Hing, MBA

## COMPANY SECRETARY

WONG Hon Sum, Hudson, FHKSA

## BERMUDA ASSISTANT SECRETARY

A.S.&K. Services Limited

## QUALIFIED ACCOUNTANT

LING Chun Kwok, Alfred, ACCA, AHKSA

## AUDIT COMMITTEE

GUO Guoqing

FAN Wan Tat

HAN K. Huang

## SPONSOR

Celestial Capital Limited

## AUDITORS

KPMG

*Certified Public Accountants*

## HEAD OFFICE AND PRINCIPAL PLACE OF BUSINESS

Office B, 21st Floor

Teda Building

87 Wing Lok Street

Hong Kong

## REGISTERED OFFICE

Cedar House

41 Cedar Avenue

Hamilton HM12

Bermuda

## HONG KONG SHARE REGISTRAR

Central Registration Hong Kong Ltd.

Rooms 1901-5, 19th Floor

Hopewell Centre

183 Queen's Road East

Hong Kong

## PRINCIPAL BANKER

The Hong Kong and Shanghai Banking

Corporation Ltd.

## GEM STOCK CODE

8186

## WEBSITE ADDRESS

[www.md23.com](http://www.md23.com)

# Chairman's Statement

I hereby present to the shareholders the annual report of the Group for the year ended 31 December 2002.

## RESULT ANALYSIS

For the year ended 31 December 2002, the Group recorded a turnover of \$49,850,000, representing an increase of 29.4% over the year of 2001. Profits attributable to shareholders were approximately \$22,979,000, which was increased of 2.6% over the year before. Basic earnings per share amounted to 2.82 Hong Kong cents, a decrease of 35% compared with 2001.

## BUSINESS REVIEW

As at 31 December 2002, the Group entered into cooperation agreements with 65 hospitals respectively in the PRC. The expanded hospital network leads to a much higher use of RFAS, which has greatly enhanced the Group's profit through the collection of more medical service fees and increase the sales of LeVeen Electrodes (射頻針) and electric plate (電極板).

In order to expedite the application of RFAS by the hospitals in the PRC, during the reviewed period, the Group continued the publication of "International Anticancer", a monthly journal to introduce the latest developments of RFAS. We have also organized 11 medical seminars and equipment exhibitions over the main cities in the PRC, inviting medical experts to demonstrate the use of RFAS. These promotional efforts have remarkably enhanced the development of the Group's business.

## BUSINESS OUTLOOK

Expanding the hospital network, enlarging the market shares in medical equipment and continue the development of anti-cancer drugs, are still the main strategies of the Group.

Cancer-treatment business is in fast growing. Innovation and research efforts are ever made for new cancer-fighting drugs and methods across the world. In light of this, various governments are expected to introduce new legislations from time to time to monitor their use. Besides, there will be more keen and tough competitors to attempt to share the market. Towards all these challenges which we are aware of, we are preparing to keep abreast of up-to-date information on advanced technology for anti-cancer in order to improve our products and services.

On top of these, the Board see diversification of business of the Group an indispensable measure to broaden the Group's client base and revenue stream. To this end, during the reviewed period, the Company has formed two new subsidiaries namely China Best Drugs Research (Nanjing) Limited ("China Best") and Sino-Innova Medical Science & Technology Co., Limited ("Sino-Innova") and entered a joint venture agreement to establish an associate namely Jiang Xi J&P Biological Products Limited ("Jiang Xi"). China Best will be principally engaged in the research and development of anti-cancer drugs and other drugs with proprietary brand name and other medicines. Sino-Innova will mainly manufacture various pharmaceutical and test instruments which are keen demand by the PRC hospitals. Jiang Xi will produce a kind of health product ("戒煙寶") which is derived from traditional Chinese medicine.

## Chairman's Statement

The Board perceived that the new subsidiaries will enlarge the development of the medical drugs and equipments of the Group. On the whole, these new activities will in turn transform into enhanced revenue stream and a broadened client base of the Group in the future.

Many of our directors and senior management are prestigious and professional doctors from the PRC and abroad, as well as a number of professionals who are well experienced in the distribution and selling of medical equipment and drugs. With these necessary expertises, and a large hospital network, advance treatment technology and an innovative business operating model, I confident the Group will have a greater success in the coming year.

### ACKNOWLEDGEMENT

I hereby express my gratitude to all the directors for their contributions, and on behalf of the Board of Directors, I would like to extend my sincere appreciation to all the shareholders, all the hospital staff, customers, suppliers and all of our staff for their continued support.

**Li Nga Kuk, James**

*Chairman*

26 March 2003

# Management Discussion and Analysis

*(Expressed in Hong Kong dollars)*

## FINANCIAL REVIEW

The Group's annual turnover for the year ended 31 December 2002 was \$49,850,000, representing an increase of 29.4% over the corresponding year in 2001. The Group's net profits attributable to shareholders amounting to \$22,979,000, representing an increase of 2.6% as compared to the corresponding year in 2001.

The increase in turnover is attributable to the Group's strategy in technology and the trainings in the application of RFAS. Through the promotion of the technology of RFAS, the applications of RFAS in cancer treatments have been increased accordingly, the revenue of the Group has been increased as well.

Despite the growth of revenue in 2002, the operating expense of the Group was also increased of 144.8% to \$12,412,000 (2001:\$5,069,000) as compared to the corresponding year in 2001. The increase in operating expense were mainly due to increase in depreciation expenses, staff costs, and donation for R&D fund.

The increase in the Group's turnover and revenue were partly offset by the increase of the operating expense and the Group's net profits attributable to shareholders was only increase of 2.6% as compared with the last year.

The basic earnings per share has decreased by 35% to 2.82 Hong Kong cents as compared with the corresponding year in 2001.

## CAPITAL STRUCTURE

On 7 August 2002, a total of 35,000,000 ordinary shares of \$0.01 each of the Company (the "Shares"), with an aggregate nominal value of \$350,000, were issued pursuant to two placing and subscription agreements both dated 24 July 2002 in relation to a top-up placing arrangement (the "Top-up Placing"). Under the Top-up Placing, a total of 35,000,000 existing Shares, of which 32,800,000 Shares and 2,200,000 Shares were then held by Mr. Li Nga Kuk, James and Mr. Li Wo Hing (both are directors and shareholders of the Company), respectively, were placed to 15 placees who were independent of and not connected with the directors, chief executives, substantial shareholders or management shareholders of the Company or any associates of any of them, at a price of \$0.57 per Share (which represented a discount of approximately 1.72% to the closing price of \$0.58 per Share as quoted on the Stock Exchange on 23 July 2002, the date immediately before the date of the above mentioned placing and subscription agreements). Following completion of such placement of existing Shares, 32,800,000 new Shares and 2,200,000 new Shares were issued to Mr. Li Nga Kuk, James and Mr. Li Wo Hing, respectively, on 7 August 2002, also at a price of \$0.57 per Share. The Board considered that the Top-up Placing would enlarge the shareholder base and the capital base of the Company and would strengthen the financial position of the Group. The relevant net proceeds received by the Group from the Top-up Placing was approximately \$19,259,000 in total, \$15,000,000 of which would be applied to finance the establishment of cancer treatment centers, and the balance of \$4,259,000 would be applied to finance the continual development of the network of hospitals in the PRC for the Group's RFAS. All net proceeds was still unused by the Group as at 31 December 2002 and have been deposited with licenced bank.

# Management Discussion and Analysis

*(Expressed in Hong Kong dollars)*

After the aforesaid issues of new Shares, as at 31 December 2002, the total number of issued Shares and the issued share capital of the Company were 835,000,000 (2001: 800,000,000) and \$8,350,000 (2001: \$8,000,000) respectively.

## FINANCIAL RESOURCES BORROWINGS, BANKING FACILITIES AND LIQUIDITY

At as 31 December 2002, the Group has still maintained its sound financial position. The Group had total assets of \$163,007,000 (2001: \$109,102,000) which were financed by current liabilities of \$28,455,000 (2001: \$16,759,000) and shareholders' equity of \$134,552,000 (2001: \$92,343,000).

The current assets of the Group amounted approximately \$147,229,000 (2001: \$98,388,000) of which approximately \$107,218,000 were cash and bank deposits (2001: \$44,165,000) due to low inventory level and good recoverability of debts. The Group had no non-current liabilities or bank loans in both year. The current liabilities of the Group amounted to approximately \$28,455,000 (2001: \$16,759,000) of which approximately \$15,786,000 (2001: \$9,994,000) were trade and other payables and \$10,212,000 (2001: \$5,196,000) was provision for taxation.

The Group generally finances its operations with internally generated resources. The Group's policy is to place surplus fund with banks on deposits with maturity within one year. None of Group's assets are charged to secure the Group's bank loan. Furthermore, the Group had no long term borrowings. The gearing ratio calculated on the basis of bank loan is nil (2001: nil).

The net asset per Share as at 31 December 2002 was \$0.16 (2001: \$0.12).

## CAPITAL COMMITMENT, SIGNIFICANT INVESTMENTS AND MATERIAL ACQUISITIONS/DISPOSALS OF SUBSIDIARIES AND AFFILIATED COMPANIES

On 6 June 2002, Tat Lung Medical Treatment Technology Limited ("Tat Lung HK"), a wholly-owned subsidiary of the Company entered into a joint venture agreement to establish an associate named as Jiang Xi ("江西健普生物制品有限公司"). It was planned to produce a kind of health product ("戒煙寶"), which is derived from traditional Chinese medicine. Tat Lung HK invested RMB490,000 which represented 49% of total registered and issued share capital of Jiang Xi.

On 4 September 2002, the Company set up a 90% owned subsidiary with registered capital of US\$2,600,000 named as Sino-Innova Medical Science & Technology Co., Limited ("神州英諾華醫療科技有限公司") to manufacture various pharmaceutical and test instruments, including Automatic Biochemical Analyzer, Automatic Immunity Analyzer, Immunity Meter, etc., which were the most wanted test instruments by the PRC hospitals at present.



# Management Discussion and Analysis

*(Expressed in Hong Kong dollars)*

On 18 September 2002, a wholly owned subsidiary named as China Best Drugs Research (Nanjing) Limited (“南京神州佳美藥物研究有限公司”) with registered capital of US\$3,000,000 was incorporated and it was principally planned to engage in the research and development of anti-cancer drugs with proprietary brand name and other medicine, such as cardiovascular treatment and respiratory system treatment medicine.

On 6 December 2002, the Company entered into an acquisition agreement with an independent third party to buy certain Medicine Research Projects. The details thereof are set out in the note 29(b)(ii) to the financial statements. As at the date of this annual report, acquisition of the Medicine Research Projects have not been completed. Upon completion of such acquisition, China Best Drugs Research (Nanjing) Limited will be the owner of such Medicine Research Projects, and the Company will hold 75% equity interest in China Best Drugs Research (Nanjing) Limited and the remaining 25% will be held indirectly by the vendor of the Medicine Research Projects. Please also refer to the circular of the Company dated 9 January 2003 for more details of the acquisition of the Medicine Research Projects.

Apart from the aforesaid, the Company held no other significant investment and made no other acquisitions/disposals of subsidiaries and affiliated companies during the year ended 31 December 2002.

As at 31 December 2002, the Group had outstanding capital commitment of approximately \$5,415,000 (2001: nil). The details information are set out in the note 29(a) of the financial statements.

## FOREIGN EXCHANGE EXPOSURE AND HEDGING INSTRUMENTS

The Group’s transactions are denominated in Renminbi, Hong Kong dollars and US dollars. During the year under review, the exchange rates of such currencies have been stable. The Group has not entered into any hedging arrangements.

As at 31 December 2002, the Group did not have outstanding hedging instruments (2001: nil).

## EMPLOYEES’ INFORMATION AND BENEFIT SCHEME FOR THE EMPLOYEES

As at 31 December 2002, the Group had 128 (2001: 60) employees. The total of employee remuneration, including that of the Directors, for the year ended 31 December 2002 and year ended 31 December 2001 amounted to \$3,223,000 and \$1,362,000 respectively. The Group’s employee are selected and promoted based on suitability for the position offered. The salary and related benefits the employees are rewarded on a performance related basis and the general remuneration structure of the Group is subject to review annually.

In addition to Share Option Scheme, the Group also provide a mandatory provident fund scheme for its staff in Hong Kong in compliance with requirements under the Mandatory Provident Fund Scheme Ordinance and pays retirement fund according to the relevant regulation of PRC.

# Management Discussion and Analysis

*(Expressed in Hong Kong dollars)*

Pursuant to the relevant labor rules and regulations in PRC, the PRC subsidiaries of the Group participate in a defined contribution retirement benefit scheme (the “Scheme”) organized by the municipal government whereby the subsidiaries are required to contribute to the Scheme to fund the retirement benefits of the eligible employees. The government of PRC is responsible for the entire pension obligations payable to retired employees. The Group is not liable to any retirement benefits payment beyond the contributions to the Scheme.

## CONTINGENT LIABILITIES

At at 31 December 2002, the Group and the Company did not have any significant outstanding contingent liabilities apart from the potential contingent liabilities arising from the Group’s operations as disclosed under the risk factors in the prospectus relating to “Products liability and limited insurance coverage”. As the liabilities relating to “Product liability and limited insurance coverage” under the Risk Factors in the Prospectus are very remote, accordingly no such disclosures are included in the financial statement.

## BUSINESS REVIEW

During the year, the Group’s turnover and operating profit are almost entirely derived from the provision of medical equipment and related accessories services to the clients in the People’s Republic of China (the “PRC”).

With the continuous growth in the number of contracted hospitals in the PRC, the provision of radio frequency therapeutic (“RFAS”) equipment and technology (“RFAS technology”) to hospitals has increased significantly which in turn contributes to our revenue and help the development of related businesses. The following is a summary of the development of the Group during the year:

### Continual development of hospital network for RFAS

- The number of radio frequency therapeutic centres for tumor (射頻腫瘤治療中心) jointly established by Tat Lung Medical Treatment Technology (Shenzhen) Limited (達隆醫療科技(深圳)有限公司), a subsidiary of the Group and the hospitals in the PRC has increased from 49 in 2001 to 65 as at 31 December 2002. The total revenue generated from RFAS treatment was \$33,620,000 and the total revenue from the sales of LeVein Electrodes (射頻針) and electric plate (電極板) was \$15,973,000 and \$257,000 respectively. The detail information are stated out in note 3 of the financial statements.

# Management Discussion and Analysis

(Expressed in Hong Kong dollars)

## Promotion of application of RFAS and establishment of RFAS training centers

- Tat Lung Medical Treatment Technology (Shenzhen) Limited (達隆醫療科技(深圳)有限公司), a subsidiary of the Group and Chengdo Military Area General Hospital (成都軍區總醫院) have established the RFAS research and treatment center for the training of RFAS application. The center has also commenced research on the next generation of RFAS equipment and the development of multi-purpose LeVeen Electrodes (射頻針). It aims to realize the domestic production of such equipment and to trim down the production cost to only one fifth of its counterpart imported from overseas. The marginal profit will be thus substantially increased. The improved equipment can better serve the needs of domestic hospitals and has more function as well. The development of the said equipment has completed and is undergoing animal test. The products have all applied for and passed the initial examination for patent from the State.
- Eleven seminars on radio frequency therapeutic technology for tumor and equipment exhibitions were successively launched in Beijing, Guangzhou, Hangzhou, Xiamen, Changsa, Fuzhou, Xuzhou, Ningbao, Jinan, Shenyang and Shenzhen in order to promote RFAS technology and equipment.
- RFAS tumor therapeutic technology training courses were provided for doctors from hospitals in Kunming, Xuzhou, Jinan, Ningbao, Wuhan and Nanchang.

## Development of the market for anti-cancer drugs and 3-dimentional laparoscope

- Established China Best Drugs Research (Nanjing) Limited (“China Best”) in Nanjing Advanced New Technolgoey Development Zone and is proceeding to acquire sixteen projects on the R&D of Chinese and western medicines. China Best has already engaged a number of specialists in drugs R&D. They will continue to develop the most suitable products to meet the market needs.
- Commence development of a brand new version of 3-dimentional laparoscope with an advanced optical engineering institute in the PRC. After repeated testing, we have decided to cooperate with one of the most renowned optical experts in the PRC to make modification based on the original design so as to better serve the market needs.
- In view of IP6 failed to obtain the final approval from the State Drug Administration (中國藥醫局) and the production cost of Neustin being too high, the board of directors, after consideration, has decided to temporarily suspend the development of those two products at the moment.

# Management Discussion and Analysis

(Expressed in Hong Kong dollars)

## Other development

- Entered into a cooperation memorandum with the medical school of Shanghai Fudan University by setting up China Best Drugs R&D Fund (神州佳美藥物研發基金). Leveraging on the R&D results of Fudan University and its abundant expertise to jointly carry out R&D and jointly registration for the Chinese and western drugs developed.
- Sino-Innova Medical Science & Technology Co., Limited (“Sino-Innova”), a Sino foreign joint equity company is being set up by the holding company, which will engage in the manufacturing of advance medical examination equipment including various biochemical analyzer, immunity analyzer, genetic analyzer and blood analyzer. Those are all basic examination devices being applied in anti-cancer treatment. They will not only be available for domestic sales but will be distributed to Europe, America, South Asia and Middle East. The factory site, with an area of approximately 8,000 square meters, is expected to be completed by the middle of 2003. At the same time, in order to have an early grasp of market share, the holding company has sent out its staff to attend various international medical equipment exhibitions which has gained initial achievement, for example, the Group currently has business connections and conducts technology exchange with Italy, Spain, United Arab Emirates and India.
- The Group has invested RMB490,000 to establish an associate of Jiang Xi (江西健普生物制品有限公司) for the production of “戒煙寶” a kind of health product. It is derived from traditional Chinese medicine and contains no chemical ingredients and is well-known for its medical effect. It is now available from over 200 pharmacies in Shenzhen and is looking for domestic and overseas distributors.
- The next generation of RFAS tumor treatment software developed by a subsidiary of the Group has obtained formal approval to be sold separately as software product. Meanwhile, research on new examination equipment software has commenced which are intended for overseas sales.
- Although the Group has evolved from a sole RFAS equipment and service provider to become a group company owning a number of medical treatment and technology companies, the business under which it conducts remain related to the medical field. The Group has fully utilized the established sales network of the Company and the well-built company image and brand image of the RFAS product in order to expand the scale of operation. The number of staff of the Group increased from 60 as at 31 December 2001 to 128, of which about 80% have attained university or higher education qualifications.

# Management Discussion and Analysis

(Expressed in Hong Kong dollars)

## Outlook and future strategies

As the medical market further expands and opens in line with the rapid development of China's economy, the Group will continue to further increase its market share by promoting the application of RFAS technology in the PRC hospitals, and, taking advantage of its existing sales and marketing networks, to develop more projects of medical services. Currently income of the Group remains concentrated and relied on two specific businesses. To ensure a long-term growth with steady concurrent income, the Group will strive to develop and expand to other related businesses other than its own business to boost its revenue. To this end it will take the following steps:

- Continuous effort will be put on the development of RFAS technology and services. The number of cooperation with hospitals will increase. Progressive steps will be taken to introduce the application of RFAS technology to small and medium size as well as remote hospitals.
- The application of RFAS technology will extend to more areas. The number of treatment case of lung cancer will increase. Taking advantage of the RFAS research institute jointly established with Chengdo Military Area General Hospital, the research and development of RFAS equipment and LeVeen Electrodes (射頻針) will continue to speed up. The propriety LeVeen Electrodes (射頻針) and RFAS equipment are expected to be launched in the fourth quarter of 2003 and the first quarter of 2004 respectively.
- Three RFAS training centers are scheduled to be built for the purpose of training more RFAS technical personnel.
- A new sample of the modified 3-dimensional laparoscope (三維腹腔鏡) is expected to be completed in the middle of 2003. A production standard formulated according to the result will be filed to the SDA for approval of clinical test.
- China Best expected to have a brand new medicine ready to report and apply for registration under Category I by the middle of 2003. The company is currently compiling all documentation work while continuing the R&D on other drugs. On top of drugs R&D, the company also conducts research and development on health care products, such as “抗癌片” and “克感片”etc. These products are expected to launch in the first half of 2003 through the existing distribution network of the Group.
- With the technical support of the Medical School of Fudan University, part of the research projects, together with the medicine research projects of China Best, will be filed for approval to the Medical School of Shanghai's Fudan University under the name of China Best Drugs Research Center, with an aim to ensure the quality of the research products and the value of the research results. Meanwhile, research and development of new topics raised by Fudan University will commence capitalizing on the university's technical facilities, with China Best Drugs Research (Nanjing) Ltd having the preference in using the results.

# Management Discussion and Analysis

*(Expressed in Hong Kong dollars)*

- It is scheduled that in the middle of 2003 Sino-Innova (神州英諾華醫療科技有限公司) will have completed the infrastructure construction of its plant facility. Further research and development will be carried out in respect of an array of equipment for testing Biochemical products to cater for the needs of domestic and overseas markets. It is expected that the filing and approval of the Large-sized Automatic Immunity Analyzer (大型全自動免疫分析儀), Large-sized Automatic Biochemical Analyzer (大型全自動生化分析儀), Immunity Meter (酶標儀), and Semi-automatic Biochemical Analyzer (半自動生化分析儀) and Blood Cell Meter (血球儀) suitable for use by small size hospitals will be completed by the end of June 2003.
- Jiang Xi (江西健普生物制品有限公司) has the intention to make Guangdong as the testing ground for the sale of “戒煙寶”. In other words, direct sales will take place between the company and pharmacies. Sales in other places, including overseas, will take the form of sales agents. It is expected that sales agents networks will be established in Mainland China and places like Taiwan, Hong Kong, the United States, the Middle East and India.
- New products will be introduced. Given the effective sales and marketing networks established by the Group in the PRC medical market, many domestic and foreign enterprises producing cancer treatment equipment and medicines and healthcare products have approached the Group for cooperation. The Group will consider the possibility of any cooperation arrangements in light of the complementary effect of their products and that with the Group, and whether the arrangement will enhance the overall competitiveness of the Group.

# Management Discussion and Analysis

(Expressed in Hong Kong dollars)

## Business Objectives in Comparison with Actual Business Progress

	<b>Projects</b>	<b>For the six months ended 31 December 2002 as disclosed in the Prospectus</b>	<b>Actual business progress for the six months ended 31 December 2002</b>
A	Continual development of the hospital cooperation network in the PRC for RFAS	Enter new cooperation contracts with 15 hospitals in Sichuan	Entered new cooperation contracts with 3 hospitals which is behind the schedule stated in the prospectus of the Company
B	Promotion of application of RFAS and establishment of RFAS training centers	Host 5 conferences to demonstrate and promote the application of RFAS	Host 5 conferences to promote RFAS
		Attended the Tenth Medical Conference for Liver Cancer Treatment in the PRC (第十屆中國肝癌治療會議)	Attended the National Conference for Liver Cancer Treatment in Hangzhou (杭州全國肝癌治療會議)
		Provide training to doctors from five contracted hospitals by the Group's consultants who are doctors and professors from the universities and hospitals in the PRC	Provided training of RFAS to doctors of six hospitals
C	Development of the market for or assisting the sales of anti-cancer drugs and 3-dimensional laparoscope	Continue to provide assistance in relation to the sale of IP6 and Neustim to the contracted hospitals in the PRC	The sale business of IP6 and Neustim has not yet commenced as IP6 failed to obtain the final approval from the State Drug Administration and the manufacturer failed to supply Neustim at the price agreed with the Group due to its high production cost. The business is temporarily suspend at the moment
		Complete the registration of the 3-dimensional laparoscope with the Drug Administration	

# Management Discussion and Analysis

(Expressed in Hong Kong dollars)

Projects	For the six months ended 31 December 2002 as disclosed in the Prospectus	Actual business progress for the six months ended 31 December 2002
D Establishment of cancer treatment centers	<p>Commence production of 3-dimensional laparoscope by contractors</p> <p>Install of medical devices to the first cancer treatment center</p> <p>Commence operation of the first cancer treatment center</p> <p>Place purchase order of the medical devices and hire 30 staff for the second cancer treatment center</p>	<p>After due investigation, consultants of the Group are of the view that prototype of the 3-dimensional laparoscope needs further modification. As a result, the Group turned to cooperate with the photoelectric medical engineering center of a sophisticated photoelectric engineering institute to produce the prototype according to the new design concept. The production of the new prototype is expected to complete by the end of May</p> <p>The project in relation to the joint establishment of the tumor treatment centers with hospitals in the PRC has been suspended. After repeat assertion and investigation, the Group considers it is not an appropriate time to inject a huge sum of money to establish this kind of treatment center. The reason is because the Group has to invest an enormous amount of capital, acquire a considerable amount of equipment and fixed assets before the treatment centers can be established. From the findings of the said assertion and investigation, the amount required to be invested is much more than originally planned. The Group, on an overall basis, considers the return from investment is not impressive and the project involves high risk. As a result, in order to be responsible to the shareholders, the Group temporarily suspended this project and subjected to further development in the future.</p>



# Management Discussion and Analysis

(Expressed in Hong Kong dollars)

## The Use of Net Proceeds Resulting From Placing of New Shares

<b>Projects</b>	<b>Amount to be used from 15 December 2001 to 31 December 2002 as disclosed in the Prospectus (million)</b>	<b>Actual amount used as at 31 December 2002 (million)</b>
A Continual development of the hospital network in the PRC for RFAS	14.7	8
B Promotion of application of RFAS and the establishment of RFAS training centers	2.4	0.8
C Development of the market for or assisting in the sales of anti- cancer drugs and 3-dimensional laparoscope	7.0	1.5
D Establishment of cancer treatment centers	23.55	-

During the period under review, the Group has spent approximately \$10,300,000 on a number of projects in line with those specified in the prospectus. The unused proceeds from the placing of shares of approximately \$49,321,000 have been deposited with licenced bank.

# Directors and Senior Executives

## DIRECTORS

### Executive Directors

**Dr. Li Nga Kuk, James**, aged 57, is an Executive Director, Chairman of the Company responsible for the strategic development of the Group. He graduated from 中國上海第二醫學院 in 1970. He was granted medical doctor's licenses in Hong Kong and doctor qualification in US in 1981 and 1987 respectively and worked as a medical doctor in the PRC and Hong Kong during 1975 to 1985. Dr. Li was appointed on 7 September 2001.

**Mr. Ng Kwai Sang**, aged 41, is an Executive Director and the Deputy Chairman of the Company responsible for the strategic development of the Group. He is currently a 廣東惠來市政協委員 (a member of the Chinese People's Political Consultation Committee in Huilai City of Guangdong Province) and a guest professor in marketing management in 中國人民大學 Renming University of China. Mr. Ng was appointed on 7 September 2001.

**Mr. Li Wo Hing**, MBA, aged 56, is an Executive Director and General Manager of the Company responsible for the daily management of the Group. He has more than 10 years' experience in the trading of medical products and investment in the PRC. Mr. Li was appointed on 7 September 2001.

**Mr. Chan Shut Li, William**, MBA, aged 49, is the an Executive Director and Vice General Manager of the Company responsible for marketing and operations of the Group. Before joining the Group, he was the Sales Manager of 丹麥寶隆洋行(中國)有限公司 (Great Asiatic Company Limited), one of the largest international enterprise in Denmark, and was the General manager of 韓國雙龍株式會社 (Ssang Yong Corporation) in Guangzhou. Mr. Chan was appointed on 7 September 2001.

**Mr. Chan Siu Sun**, aged 48, is an Executive Director and Vice General Manager of the Company, responsible for the product development of the Group. Before joining the Group, he was the General Manager of 金寶威強有限公司 Glitter Power Limited and the General Manager of 湖南金樂醫藥實業有限公司 Hunan Jinle Medical Industrial Co., Ltd.. This Company is a joint venture enterprise of pharmaceutical manufacturer. Mr. Chan was appointed on 7 September 2001.

**Dr. Li Tai To, Titus**, aged 63, is an Executive Director and Vice General Manager of the Company responsible for promoting the RFA technology in the PRC. He graduated from 中國上海第一醫學院 and has obtained a medical diploma in Taiwan. He was a surgeon in 浙江嘉興第二醫院 (Zhejiang Jiaying No. 2 Hospital). Dr. Li is elder brother of Mr. Li Nga Kuk, James, the Chairman of the Company. Mr. Li was appointed on 7 September 2001.

## Directors and Senior Executives

### Non-executive Director

**Dr. Chen Min Shan**, aged 38, is a non-executive Director. Dr. Chen is a medical doctor and an associate professor, Hepatobiliary Department, Tumor Hospital, Zhong Shan Medical University. Dr. Chen was appointed on 10 December 2001.

### Independent non-executive Directors

**Mr. Han K. Huang**, aged 63, is an independent non-executive Director. Mr. Huang is a professor of School of Medicine University of Southern California, the United States and the chair professor of Medical Informatics Department of Optometry and Radiography. The Hong Kong Polytechnic University. Mr. Han was appointed on 10 December 2001.

**Mr. Fan Wan Tat**, aged 58, is an independent non-executive Director. Mr. Fan is a medical doctor in Hong Kong. Mr. Fan was appointed on 10 December 2001.

**Mr. Guo Guoqing**, aged 40, is an independent non-executive Director. Mr. Guo is the president of Commercial College, Zhongguo Renmin University. Mr. Guo was appointed on 10 December 2001.

## SENIOR MANAGEMENT

### Consultants

**Dr. Chen Min Shan**, aged 38, is a consultant of the Company. Dr. Chen is medical doctor at the Tumor Hospital, Zhongshan University, Guangzhou, the PRC. Dr. Chen joined the Group in July 2001.

**Mr. Tian Fu Zhou**, aged 59, is a consultant of the Company. Mr. Tian is a professor of the Military Hospital of Chengdu, the PRC. He joined the Group in July 2001.

**Mr. Wang Guang Tian**, aged 66, is a consultant of the Company. Mr. Wang is a professor of the Affiliate Hospital of Henan Medical University, the PRC. He joined the Group in July 2001.

# Report of the Directors

The directors hereby present the annual report together with the audited financial statements of Medical China Limited (“the Company”) and its subsidiaries (together with the “Group”) for the year ended 31 December 2002.

## PRINCIPAL ACTIVITIES

The principal activity of the Company is investment holding and the Group is principally engaged in the provision of medical equipment and related accessories services in the People’s Republic of China (“the PRC”). The principal activities and other particulars of its subsidiaries are set out in note 13 to the financial statements.

The Group’s turnover for the year is principally attributable to the provision of medical equipment, net of business tax and the sales value of medical accessories to customers, net of value added tax. An analysis of the turnover from the principal activities during the financial year are set out in note 3 to the financial statements.

## FINANCIAL STATEMENTS

The profit of the Group for the year ended 31 December 2002 and the state of the Company’s and the Group’s affairs as at that date are set out in the financial statements on pages 27 to 67.

## DIVIDENDS AND RESERVES

The directors do not recommend the payment of any final dividend for the year ended 31 December 2002.

Details of the movements in reserves of the Group and the Company during the year are set out in note 27 to the financial statements.

# Report of the Directors

## MAJOR CUSTOMERS AND SUPPLIERS

	Percentage of the Group's total	
	Sales	Purchases
The largest customer	5%	–
Five largest customers in aggregate	18%	–
The largest supplier	–	77%
Five largest suppliers in aggregate	–	100%

At no time during the year have the directors, their associates or any shareholders of the Company (which to the knowledge of the directors owns more than 5% of the Company's share capital) had any interest in these major customers and suppliers.

## DONATIONS

Donations made by the Group during the year amounted to HK\$1,055,000 (2001: Nil).

## FIXED ASSETS

Details of the movements in fixed assets of the Group during the year are set out in note 11 to the financial statements.

## SHARE CAPITAL

Details of the movements in share capital of the Company during the year are set out in note 26 to the financial statements.

## BANK LOANS AND OTHER BORROWINGS

The Company and the Group had no bank loans and other borrowings as at 31 December 2002.

# Report of the Directors

## DIRECTORS

The directors during the financial year and up to date of this report were:

### Executive Directors

Dr. Li, Nga Kuk James, *Chairman*

Mr. Ng, Kwai Sang

Mr. Li, Wo Hing

Mr. Chan, Shut Li William

Mr. Chan, Siu Sun

Dr. Li, Tao To Titus

### Non-executive Director

Dr. Chen Minshan

### Independent and Non-executive Directors

Mr. Guo Guoqing

Mr. Fan Wan Tat

Mr. Han K. Huang

Pursuant to the By-Laws of the Company, Messrs. Li Nga Kuk James, Ng Kwai Sang and Li Wo Hing will retire from the board by rotation at the forthcoming annual general meeting and, being eligible, offer themselves for re-election.

The biographical details of directors are set out in pages 17 to 18.

## DIRECTORS' SERVICE CONTRACTS

On 14 December 2001, all the executive directors entered into a service contract with the Company for an initial term of three years effective from 1 December 2001. The executive directors are committed by the respective service contracts to devote himself exclusively and diligently to the business and interests of the Group and to keep the Board promptly and fully informed of his conduct of business affairs, among other commitments.

The service contracts of the existing independent non-executive directors were for a term of one year commencing on 1 December 2001 and will subject to renew by the approval in the forth coming Annual General Meeting of shareholders of the Company.

## Report of the Directors

### DIRECTORS' INTERESTS IN SECURITIES

At 31 December 2002, referring to the register kept under Section 29 of the Securities (Disclosure of Interests) Ordinance (“SDI Ordinance”), the interests of the Company’s directors and their associates in shares of the Company or any associated corporations (as defined in the SDI Ordinance) were as follows:

Name of Director	Personal interest	Family interests	Corporate interests	Other interests	Total
Li Nga Kuk, James	32,800,000	–	–	–	32,800,000
Li Tai To, Titus	16,400,000	–	–	–	16,400,000
Li Wo Hing	32,800,000	–	212,320,000	–	245,120,000
			(Note 1)		
Ng Kwai Sang	32,800,000	–	212,320,000	–	245,120,000
			(Notes 1 & 2)		
Chan Siu Sun	32,800,000	–	–	–	32,800,000

Notes:

- By a letter of undertaking dated 14 December 2001, Mr. Ng Kwai Sang undertook to grant a right of first refusal to Mr. Li Wo Hing regarding his 5% shareholding in the share capital of People Market Management Limited (“PMM”), which is in turn owned as to 28.57% by Mr. Li Wo Hing. Therefore, Mr. Li Wo Hing is deemed to be interested in 212,320,000 shares held directly by PMM.
- 212,320,000 shares are owned by PMM, which is in turn owned as to 35.71% by Mr. Ng Kwai Sang.

Save as disclosed above, as at 31 December 2002, none of the directors or chief executive or their associates had any personal, family, corporate or other interests in the securities of the Company or any of its associated corporations as defined in the SDI Ordinance.

### SHARE OPTION SCHEME

Pursuant to a written resolution passed by all the shareholders of the Company on 14 December 2001, the Company had conditional approved and adopted a share option scheme (“the Share Option Scheme”).

The principal terms of the Share Option Scheme are set out in the Company’s prospectus dated 19 December 2001.

During the year no option was granted by the Company under the Share Option Scheme. As at 31 December 2002, there was no outstanding option.

# Report of the Directors

## DIRECTORS' RIGHTS TO ACQUIRE SHARES OR DEBT SECURITIES

On 14 December 2001, the Company had conditionally approved and adopted the Share Option Scheme pursuant to which any employees and directors of the Company and its subsidiaries may be granted options to subscribe for Shares of the Company under the Share Option Scheme.

As at 31 December 2002, none of the directors or chief executive or their associates had any interest or rights to subscribe for any securities of the Company or any of its associated corporations as defined in the SDI Ordinance.

At no time during the year was the Company or any of its subsidiaries or its holding company a party to any arrangement to enable the Company's directors or chief executive of the Company or any of their spouses or children under eighteen years of age to acquire benefits by means of the acquisition of shares in or debentures of the Company or any other body corporate.

## SUBSTANTIAL SHAREHOLDERS

Other than interests disclosed above in respect of directors and their associates, as at 31 December 2002, according to the register of interests kept by the Company under section 16(1) of the SDI Ordinance, the following persons were interested in 10 percentage or more of the issued share capital of the Company:

Name	No of issued share	Percentage of shareholding
PMM ( <i>note</i> )	212,320,000	25.43%
China Equity Associates L.P.	116,720,000	13.98%

*Note:* PMM is beneficially owned as to 35.71% by Mr. Ng Kwai Sang, 28.57% by Mr. Li Wo Hing, 17.86% by Dr. Li Nga Kuk, James, 8.93%, by Mr. Li Tai To, Titus and 8.93% by Mr. Li Yue Erh.

## DIRECTORS' INTERESTS IN CONTRACTS

No contract, commitment or agreement of significance in relation to the Company's business, to which the Company or any of its subsidiaries was a party and in which any of the directors of the Company had a material interest, either directly or indirectly, subsisted at the end of the year or at any time during the year.



## Report of the Directors

### **PURCHASE, SALE OR REDEMPTION OF THE COMPANY'S LISTED SECURITIES**

Neither the Company nor any of its subsidiaries purchased, redeemed or sold any of the Company's listed securities during the year ended 31 December 2002.

### **PRE-EMPTIVE RIGHTS**

There is no provision for pre-emptive rights under the Company's By-Laws or the laws in Bermuda.

### **PENSION SCHEMES**

Details of the Group's pension scheme for the year ended 31 December 2002 are set out in note 30 to the financial statements.

### **COMPLIANCE WITH RULES 5.28 TO 5.39 OF THE GEM LISTING RULES**

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 during the year.

### **AUDIT COMMITTEE**

As required by the Rule 5.23 of the GEM Listing Rules, the Company has established an audit committee ("Committee") with written terms of reference which deal with its authority and duties. The Committee's primary duties are to review and to supervise the financial reporting process and internal control system of the Group and to provide advice and comments to the directors.

The Committee comprises three independent non-executive directors, namely Messrs. Guo Guoqing, Fan Wan Tai and Han K. Huang. The committee held three meetings during the year.

The Audit Committee Members have reviewed the annual report for the year ended 31 December 2002.

# Report of the Directors

## INTEREST OF SPONSOR

As at 31 December 2002, the Sponsor of the Company, Celestial Capital Limited, its directors, employees and its associates did not have any interest in the securities of the Company or any subsidiaries of the Group, or any right to subscribe for or to nominate persons to subscribe for the securities of the Company or any member of the Group.

Celestial Capital Limited has entered into a sponsorship agreement with the Company whereby, for a fee, Celestial Capital Limited will act as the Company's continuing sponsor for the period from 31 December 2001 to 31 December 2003.

## AUDITORS

The financial statements for the year were audited by KPMG, Certified Public Accountants. KPMG will retire at the conclusion of the forthcoming Annual General Meeting, and being eligible, will offer themselves for re-appointment. A resolution for the re-appointment of KPMG as auditors of the Company is to be proposed at the forthcoming Annual General Meeting.

By order of the Board  
**Li Nga Kuk, James**  
*Chairman*

Hong Kong, 26 March 2003

# Auditors' Report



To the shareholders of  
**Medical China Limited**  
*(Incorporated in Bermuda with limited liability)*

We have audited the financial statements on pages 27 to 67 which have been prepared in accordance with accounting principles generally accepted in Hong Kong.

## RESPECTIVE RESPONSIBILITIES OF DIRECTORS AND AUDITORS

The Company's directors are responsible for the preparation of financial statements which give a true and fair view. In preparing financial statements which give a true and fair view it is fundamental that appropriate accounting policies are selected and applied consistently, that judgements and estimates are made which are prudent and reasonable and that the reasons for any significant departure from applicable accounting standards are stated.

It is our responsibility to form an independent opinion, based on our audit, on those financial statements and to report our opinion to you.

## BASIS OF OPINION

We conducted our audit in accordance with Statements of Auditing Standards issued by the Hong Kong Society of Accountants. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the Company's and the Group's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance as to whether the financial statements are free from material misstatement. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements. We believe that our audit provides a reasonable basis for our opinion.

## OPINION

In our opinion, the financial statements give a true and fair view of the state of affairs of the Company and of the Group as at 31 December 2002 and of the Group's profit and cash flows for the year then ended and have been properly prepared in accordance with accounting principles generally accepted in Hong Kong and the disclosure requirements of the Hong Kong Companies Ordinance.

**KPMG**  
*Certified Public Accountants*

Hong Kong, 26 March 2003

# Consolidated Income Statement

For the year ended 31 December 2002  
(Expressed in Hong Kong dollars)

	Note	2002 \$'000	2001 \$'000
<b>Turnover</b>	3	<b>49,850</b>	38,523
Cost of services/sales		<b>(14,592)</b>	(9,415)
<b>Gross profit</b>		<b>35,258</b>	29,108
Other revenue	4	<b>4,814</b>	2,897
Other net income/(loss)	4	<b>327</b>	(10)
Selling and distribution expenses		<b>(4,481)</b>	(1,952)
Administrative expenses		<b>(7,853)</b>	(2,869)
Other operating expenses		<b>(78)</b>	(238)
<b>Profit from operations</b>		<b>27,987</b>	26,936
Finance cost	5(a)	–	(316)
Share of loss of associate		<b>(15)</b>	–
<b>Profit before taxation</b>	5	<b>27,972</b>	26,620
Taxation	6(a)	<b>(4,993)</b>	(4,217)
<b>Profit attributable to shareholders</b>	9	<b>22,979</b>	22,403
<b>Earnings per share (in Hong Kong cents)</b>			
Basic	10	<b>2.82</b>	4.34
Diluted		<b>N/A</b>	3.45

The notes on pages 34 to 67 form part of these financial statements.

## Consolidated Balance Sheet

At 31 December 2002

(Expressed in Hong Kong dollars)

	Note	2002		2001	
		\$'000	\$'000	\$'000	\$'000
<b>Non-current assets</b>					
Fixed assets	11(a)				
– Property, plant and equipment			22,608		22,420
Construction in progress	12		1,547		–
Interest in an associate	14		447		–
Negative goodwill	15		(8,824)		(11,706)
			15,778		10,714
<b>Current assets</b>					
Inventories	16	1,648		868	
Trade receivables	17	3,398		2,105	
Other receivables and prepayments	19	34,557		51,250	
Amount due from a related company	20	408		–	
Deposits with banks	21	93,488		16,972	
Cash and cash equivalents	22	13,730		27,193	
		147,229		98,388	
<b>Current liabilities</b>					
Trade and other payables	23	15,786		9,994	
Amount due to a related company	24	897		897	
Amount due to a director	25	1,560		672	
Taxation	6(b)	10,212		5,196	
		28,455		16,759	
<b>Net current assets</b>			<b>118,774</b>		<b>81,629</b>
<b>NET ASSETS</b>			<b>134,552</b>		<b>92,343</b>

# Consolidated Balance Sheet

At 31 December 2002  
(Expressed in Hong Kong dollars)

	Note	2002		2001	
		\$'000	\$'000	\$'000	\$'000
<b>CAPITAL AND RESERVES</b>					
Share capital	26		8,350		8,000
Reserves	27(a)		126,202		84,343
			134,552		92,343

Approved and authorised for issue by the board of directors on 26 March 2003.

**Li Nga Kuk, James**  
*Chairman*

**Li Wo Hing**  
*Director*

The notes on page 34 to 67 form part of these financial statements.

# Balance Sheet

At 31 December 2002

(Expressed in Hong Kong dollars)

	Note	2002		2001	
		\$'000	\$'000	\$'000	\$'000
<b>Non-current assets</b>					
Fixed assets	11(b)		729		–
Investments in subsidiaries	13		14,830		5,465
			15,559		5,465
<b>Current assets</b>					
Amounts due from subsidiaries	18	27,891		13,012	
Other receivables and prepayments	19	30,836		47,664	
Cash and cash equivalents	22	8,657		2,729	
		67,384		63,405	
<b>Current liabilities</b>					
Trade and other payables	23	2,044		2,665	
Amount due to a subsidiary	18	507		1,175	
Amount due to a director	25	1,560		672	
		4,111		4,512	
<b>Net current assets</b>			<b>63,273</b>		<b>58,893</b>
<b>NET ASSETS</b>			<b>78,832</b>		<b>64,358</b>
<b>CAPITAL AND RESERVES</b>					
<b>Share capital</b>	26		<b>8,350</b>		<b>8,000</b>
<b>Reserves</b>	27(b)		<b>70,482</b>		<b>56,358</b>
			<b>78,832</b>		<b>64,358</b>

Approved and authorised for issue by the board of directors on 26 March 2003.

**Li Nga Kuk, James**  
Chairman

**Li Wo Hing**  
Director

The notes on pages 34 to 67 form part of these financial statements.

## Consolidated Statement of Changes in Equity

For the year ended 31 December 2002  
(Expressed in Hong Kong dollars)

	Note	2002		2001	
		\$'000	\$'000	\$'000	\$'000
Shareholders' equity at 1 January			92,343		4,851
Net (losses)/gains not recognized in the income statement					
– Exchange differences on translation of the financial statements of foreign entities	27(a)		(29)		10
Net profit for the year			22,979		22,403
Movements in share capital:					
Issue of share capital		19,259		59,814	
Reorganization adjustment		–		5,265	
Net increase in shareholders' equity arising from capital transactions with shareholders			19,259		65,079
Shareholders' equity at 31 December			134,552		92,343

The notes on pages 34 to 67 form part of these financial statements.



## Consolidated Cash Flow Statement

For the year ended 31 December 2002

(Expressed in Hong Kong dollars)

	Note	2002		2001	
		\$'000	\$'000	\$'000	\$'000
<b>Operating activities</b>					
Profit before taxation		27,972		26,620	
Adjustments for:					
Depreciation		4,722		3,772	
Amortization of negative goodwill		(2,882)		(2,882)	
Profit on disposal of fixed assets		(327)		–	
Interest income		(1,898)		(15)	
Finance cost		–		316	
Share of losses of an associate		15		–	
Foreign exchange (gain)/loss		(6)		10	
<b>Operating profit before changes in working capital</b>					
		27,596		27,821	
Increase in inventories		(780)		(868)	
Increase in trade receivables		(1,293)		(1,081)	
Decrease/(Increase)in other receivables and prepayments		12,997		(1,326)	
Increase in trade and other payables		5,792		10,575	
(Increase)/decrease in amount due from a related company		(408)		7,027	
Increase in amount due to a related company		–		898	
Increase in amount due to a director		888		672	
<b>Cash generated from operation</b>					
		44,792		43,718	
Income tax paid outside Hong Kong		–		(9)	
<b>Net cash from operating activities</b>					
		44,792		43,709	

# Consolidated Cash Flow Statement

For the year ended 31 December 2002  
(Expressed in Hong Kong dollars)

	Note	2002		2001	
		\$'000	\$'000	\$'000	\$'000
<b>Investing activities</b>					
Capital expenditure					
Fixed assets		(5,341)		(7,139)	
Construction in progress		(1,547)		–	
Placement of time deposits with banks		(76,516)		(16,972)	
Payment for acquisition of business	28(b)	–		(4,714)	
Deposit for acquisition of research projects		(30,218)		–	
Interest received		1,350		15	
Proceeds from sales of fixed assets		758		–	
Repayment from/(advances to) third party		34,462		(34,462)	
Payment for purchase of interest in an associate		(462)		–	
<b>Net cash used in investing activities</b>			<b>(77,514)</b>		<b>(63,272)</b>
<b>Financing activities</b>					
Net proceeds from issuance of new shares		19,259		46,422	
<b>Net cash generated from financing activities</b>			<b>19,259</b>		<b>46,422</b>
<b>Net (decrease)/increase in cash and cash equivalents</b>			<b>(13,463)</b>		<b>26,859</b>
<b>Cash and cash equivalents at 1 January</b>			<b>27,193</b>		<b>334</b>
<b>Cash and cash equivalents at 31 December</b>	22		<b>13,730</b>		<b>27,193</b>

The notes on pages 34 to 67 form part of these financial statements.

# Notes to the Financial Statements

(Expressed in Hong Kong dollars)

## 1. BACKGROUND OF THE COMPANY

The Company was incorporated in Bermuda on 15 August 2001 as an exempted company with limited liability under the Companies Act of Bermuda. The Company acts as an investment holding company and the Group is principally engaged in the provision of medical equipment and related accessories services in the People's Republic of China ("PRC").

## 2. SIGNIFICANT ACCOUNTING POLICIES

### (a) Statement of compliance

These financial statements have been prepared in accordance with all applicable Statements of Standard Accounting Practice and Interpretations issued by the Hong Kong Society of Accountants, accounting principles generally accepted in Hong Kong and the disclosure requirements of the Hong Kong Companies Ordinance.

These financial statements also comply with the applicable disclosure provisions of the Rules Governing the Listing of Securities of the Growth Enterprise Market ("the GEM") of the Stock Exchange of Hong Kong Limited. A summary of the significant accounting policies adopted by the Group is set out below.

### (b) Basis of preparation of the financial statements

The measurement basis used in the preparation of the financial statements is historical cost.

### (c) Basis of consolidation

The group financial statements incorporate the financial statements of Medical China Limited and all of its subsidiaries made up to 31 December each year, together with the Group's share of the results for the year and the relevant share of the post acquisition results of its associates.

### (d) Negative goodwill

Negative goodwill represents the excess of the aggregate fair value ascribed to the separable net tangible assets acquired over purchase consideration and is amortized on a straight-line basis in accordance with the remaining estimated useful economic lives of the relevant assets acquired.

# Notes to the Financial Statements

(Expressed in Hong Kong dollars)

## 2. SIGNIFICANT ACCOUNTING POLICIES (continued)

### (e) Investments in subsidiaries

A subsidiary is an enterprise in which the Group, directly or indirectly, holds more than half of the issued share capital, or controls more than half the voting power, or controls the composition of the board of directors. Subsidiaries are considered to be controlled if the Company has the power, directly or indirectly, to govern the financial and operating policies, so as to obtain benefits from their activities.

An investment in a subsidiary is consolidated into the consolidated financial statements.

Intra-group balances and transactions, and any unrealized profits arising from intra-group transactions, are eliminated in full in preparing the consolidated financial statements. Unrealized losses resulting from intra-group transactions are eliminated in the same way as unrealized gains, but only to the extent that there is no evidence of impairment.

In the Company's balance sheet, an investment in a subsidiary is stated at cost less any impairment losses (see note 2(i)).

### (f) Interest in associate

An associate is an entity in which the Group or Company has significant influence, but not control or joint control, over its management, including participation in the financial and operating policy decisions.

An investment in an associate is accounted for in the consolidated financial statements under the equity method and is initially recorded at cost and adjusted thereafter for the post acquisition change in the Group's share of the associate's net assets. The consolidated income statement reflects the Group's share of the post-acquisition results of the associates for the year.

Unrealized profits and losses resulting from transactions between the Group and its associates are eliminated to the extent of the Group's interest in the associate, except where unrealized losses provide evidence of an impairment of the asset transferred, in which case they are recognized immediately in the income statement.

# Notes to the Financial Statements

(Expressed in Hong Kong dollars)

## 2. SIGNIFICANT ACCOUNTING POLICIES (continued)

### (g) Fixed assets and depreciation

#### (i) Valuation

Fixed assets, other than construction in progress, are stated in the balance sheets at cost less accumulated depreciation (see note 2(g)(iii)) and impairment losses (see note 2(i)). Cost of an asset comprises its purchase price and directly attributable costs of bringing the assets to working condition and location for its intended use.

#### (ii) Subsequent expenditure

Subsequent expenditure relating to a fixed asset that has already been recognized is added to the carrying amount of the asset when it is probable that future economic benefits, in excess of the originally assessed standard of performance of the existing assets, will flow to the Group. All other subsequent expenditure is recognized as an expense in the period in which it is incurred.

#### (iii) Depreciation

Depreciation is calculated to write off the cost of fixed assets on a straight-line basis over the estimated useful lives as follows:

Medical equipment	Shorter of 6 years and the remaining terms of the agreements with hospitals
Office, computer and other equipment	5 years
Motor vehicles	5 years

#### (iv) Disposals

Gains or losses arising from the retirement or disposal of a fixed asset are determined as the difference between the estimate net disposal proceeds and the carrying amount of the asset and are recognized in the income statement on the date of retirement or disposal.

# Notes to the Financial Statements

(Expressed in Hong Kong dollars)

## 2. SIGNIFICANT ACCOUNTING POLICIES (continued)

### (h) Construction in progress

Construction in progress is stated at cost, which comprises construction expenditure, including interest costs and foreign exchange differences on related borrowed funds to the extent that they are regarded as an adjustment to interest costs during the construction period, and the cost of related equipment. Capitalisation of these costs ceases and the construction in progress is transferred to fixed assets when the asset is substantially ready for its intended use, notwithstanding any delays in the issue of the relevant commissioning certificate by the appropriate authorities.

No depreciation is provided in respect of construction in progress. Upon completion and commissioning for operation, depreciation will be provided at the appropriate rates specified in note 2(g)(iii) above.

### (i) Impairment of assets

Internal and external sources of information are reviewed at each balance sheet date to identify indications that the following assets may be impaired or an impairment loss previously recognized no longer exists or may have decreased:

- fixed assets;
- construction in progress; and
- investments in subsidiaries and associate.

If any such indication exists, the asset's recoverable amount is estimated. An impairment loss is recognized whenever the carrying amount of an asset exceeds its recoverable amount.

#### (i) Calculation of recoverable amount

The recoverable amount of an asset is the greater of its net selling price and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of time value of money and the risks specific to the asset. Where an asset does not generate cash inflows largely independent of those from other assets, the recoverable amount is determined for the smallest group of assets that generates cash inflows independently (i.e. a cash-generating unit).

# Notes to the Financial Statements

(Expressed in Hong Kong dollars)

## 2. SIGNIFICANT ACCOUNTING POLICIES (continued)

### (i) Impairment of assets (continued)

#### (ii) Reversals of impairment losses

An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount.

A reversal of impairment losses is limited to the asset's carrying amount that would have been determined had no impairment loss been recognized in prior years. Reversals of impairment losses are credited to the income statement in the year in which the reversals are recognized.

### (j) Inventories

Inventories are stated at the lower of cost and net realizable value.

Cost is calculated using the weighted average cost formula and comprises all costs of purchase, costs of conversion and other costs incurred in bringing the inventories to their present location and condition.

Net realizable value is the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sale.

When inventories are sold, the carrying amount of those inventories is recognized as an expense in the period in which the related revenue is recognized. The amount of any write-down of inventories to net realizable value and all losses of inventories are recognized as an expense in the period the write-down or loss occurs. The amount of any reversal of any write-down of inventories, arising from an increase in net realizable value, is recognized as a reduction in the amount of inventories recognized as an expense in the period in which the reversal occurs.

### (k) Cash equivalents

Cash and cash equivalents comprise cash at bank and on hand, demand deposits with banks and other financial institutions, and short-term, highly liquid investments that are readily convertible into known amounts of cash and which are subject to an insignificant risk of changes in value, having been within three months of maturity at acquisition. Bank overdrafts that are repayable on demand and form an integral part of the Group's cash management are also included as a component of cash and cash equivalents for the purpose of the cash flow statement.

# Notes to the Financial Statements

(Expressed in Hong Kong dollars)

## 2. SIGNIFICANT ACCOUNTING POLICIES (continued)

### (l) Deferred taxation

Deferred taxation is provided using the liability method in respect of the taxation effect arising from all material timing differences between the accounting and tax treatment of income and expenditure, which are expected with reasonable probability to crystallize in the foreseeable future.

Future deferred tax benefits are not recognized unless their realization is assured beyond reasonable doubt.

### (m) Provisions and contingent liabilities

Provisions are recognized for liabilities of uncertain timing or amount when the Company or Group has legal or constructive obligation arising as a result of a past event, it is probable that an outflow of economic benefits will be required to settle the obligation and a reliable estimate can be made. Where the time value of money is material, provisions are stated at the present value of the expenditures expected to settle the obligation.

When it is not probable that an outflow of economic benefits will be required, or the amount cannot be estimated reliably, the obligation is disclosed as a contingent liability, unless the probability of outflow of economic benefits is remote. Possible obligations, whose existence will only be confirmed by the occurrence or non-occurrence of one or more future events are also disclosed as contingent liabilities unless the probability of outflow of economic benefits is remote.

### (n) Revenue recognition

Provided it is probable that the economic benefits will flow to the Group and the revenue and costs, if applicable, can be measured reliably, revenue is recognized in the income statement as follows:

#### (i) Medical service fee

Medical service fee is recognized at the time when services are rendered, net of business tax.



# Notes to the Financial Statements

(Expressed in Hong Kong dollars)

## 2. SIGNIFICANT ACCOUNTING POLICIES (continued)

### (n) Revenue recognition (continued)

#### (ii) Sales of goods

Revenue is recognized when medical accessories are delivered at the customers' premises which is taken to be the point in time when the customer has accepted the goods and the related risks and rewards of ownership. Revenue excludes value added tax and is after deduction of any trade discounts.

#### (iii) Interest income

Interest income from bank deposits is accrued on a time-apportioned basis by reference to the principal outstanding and the rate applicable.

### (o) Operating leases

Rentals payable under the operating leases are accounted for in the income statement on a straight line basis over the period of the respective leases.

### (p) Employee benefits

(i) Salaries, annual bonuses, paid annual leave, leave passage and the cost to the Group of non-monetary benefits are accrued in the year in which the associated services are rendered by employees of the Group. Where payment or settlement is deferred and the effect would be material, these amounts are stated at their present values.

(ii) The Group's contributions to retirement benefit schemes are charged to the income statement as and when incurred. Further information is set out in note 30.

### (q) Research and development costs

Research and development costs comprise costs that are directly attributable to research and development activities or that can be allocated on a reasonable basis to such activities. Because of the nature of the Group's research and development activities, no development costs satisfy the criteria for the recognition of such costs as an asset. In the circumstances, research and development costs are recognized as expenses in the period in which they are incurred.

# Notes to the Financial Statements

*(Expressed in Hong Kong dollars)*

## 2. SIGNIFICANT ACCOUNTING POLICIES (continued)

### (r) Translation of foreign currencies

Foreign currency transactions during the year are translated into Hong Kong dollars at the exchange rates ruling at the transaction dates. Monetary assets and liabilities denominated in foreign currencies are translated into Hong Kong dollars at the exchange rates ruling at the balance sheet date. Exchange gains and losses are dealt with in the income statement.

The results of subsidiaries outside Hong Kong are translated into Hong Kong dollars at the average exchange rates for the year; balance sheet items are translated at the rates of exchange ruling at the balance sheet date. The resulting exchange differences are dealt with as a movement in reserves.

### (s) Borrowing costs

Borrowing costs are expensed in the income statement in the period in which they are incurred, except to the extent that they are capitalized as being directly attributable to the acquisition, construction or production of an asset which necessarily take a substantial period of time to get ready for its intended use or sale.

### (t) Related parties

For the purposes of these financial statements, parties are considered to be related to the Group if the Group has the ability, directly or indirectly, to control the party or exercise significant influence over the party in making financial and operating decisions, or vice versa, or where the Group and the party are subject to common control or common significant influence. Related parties may be individuals or other entities.

# Notes to the Financial Statements

(Expressed in Hong Kong dollars)

## 3. TURNOVER

Turnover represents service fees arising from the provision of medical equipment, net of business tax and the sales value of medical accessories to customers, net of value added tax.

Pursuant to various agreements with hospitals in the PRC, the Group agrees to provide certain medical equipment at the relevant hospitals and in return, share the medical service fees arising from the utilization of the medical equipment after deducting the related direct expenses.

Turnover recognized during the year may be analyzed as follows:

	2002	2001
	\$'000	\$'000
Medical service fees	33,620	28,921
Sales of Le Veen Electrodes	15,973	8,968
Sale of electric plates	257	634
	<b>49,850</b>	38,523

The Group's turnover and operating profit are almost entirely derived from the provision of medical equipment and related accessories services in the PRC. Accordingly, no segmental analysis is provided.

## 4. OTHER REVENUE AND NET INCOME/(LOSS)

	2002	2001
	\$'000	\$'000
<b>Other revenue</b>		
Interest income	1,898	15
Amortization of negative goodwill	2,882	2,882
Others	34	-
	<b>4,814</b>	2,897
<b>Other net income/(loss)</b>		
Net gain on sale of fixed assets	327	-
Exchange loss	-	(10)
	<b>327</b>	(10)

# Notes to the Financial Statements

(Expressed in Hong Kong dollars)

## 5. PROFIT BEFORE TAXATION

Profit before taxation is arrived at after charging:

	2002	2001
	\$'000	\$'000
(a) Finance cost:		
Interest expense on convertible loan	–	316
(b) Staff costs:		
Staff costs (including directors' remuneration in note 7)		
– wages and salaries	3,090	1,244
– staff retirement benefits*	133	118
	<b>3,223</b>	1,362
Average number of employees during the year	<b>128</b>	60

\* At 31 December 2002, there were no forfeited contributions available to the Group to reduce contributions of the staff retirement scheme in future years (2001: nil).

	2002	2001
	\$'000	\$'000
(c) Other items:		
Cost of inventories	10,082	5,686
Depreciation	4,722	3,772
Auditors' remuneration		
– audit services	662	662
– other services	200	–
Operating lease charges in respect of office premises	712	476
Donation	1,055	–
Research and development costs	188	186

# Notes to the Financial Statements

(Expressed in Hong Kong dollars)

## 6. TAXATION

(a) Taxation in the consolidated income statement represents:

	2002 \$'000	2001 \$'000
PRC income tax	4,993	4,217

(i) *Hong Kong Profits Tax*

No provision for Hong Kong Profits Tax has been made as the Group did not have assessable profits subject to Hong Kong Profits Tax during the year.

(ii) *PRC Income Tax*

The Company's subsidiary, Tat Lung Medical Treatment Technology (Shenzhen) Limited ("Tat Lung Shenzhen"), located in the Shenzhen Special Economic Zone in the PRC, is subject to PRC income tax at a reduced rate of 15% (2001: 15%).

During the year, the Company set up two subsidiaries, China Best Drugs Research (Nanjing) Limited ("China Best") and Sino-Innova Medical Science & Technology Company Limited ("Sino-Innova"). No provision for PRC Income Tax has been made for these two subsidiaries as they did not have assessable profits for the year determined in accordance with relevant income tax rules and regulations in the PRC.

(iii) No provision for deferred taxation has been made as the effect of all timing differences is immaterial.

(b) Taxation in the consolidated balance sheet represents:

	2002 \$'000	2001 \$'000
Provision for PRC income tax	4,993	4,217
PRC income tax paid	–	–
	4,993	4,217
Balance of PRC income tax provision relating to prior years	5,219	979
Tax payable	10,212	5,196

# Notes to the Financial Statements

(Expressed in Hong Kong dollars)

## 7. DIRECTORS' REMUNERATION

Directors' remuneration disclosed pursuant to section 161 of the Hong Kong Companies Ordinance is as follows:

	2002 \$'000	2001 \$'000
<b>Executive directors</b>		
Fees	–	–
Salaries and other emoluments	990	389
Retirement benefit scheme contributions	26	16
Bonus	83	–
	<b>1,099</b>	405
<b>Non-executive directors</b>		
Fees	240	20

The remuneration of the directors is within the following bands:

	2002 Number of directors	2001 Number of directors
Nil – \$1,000,000	10	10

During the year, no emoluments were paid by the Group to the Directors as an inducement to join or upon joining the Group or as compensation for loss of office.

The executive directors entered into service contracts with the Company for an initial period of three years commencing on 1 December 2001, and will continue thereafter unless and until, after the expiry of the first year of service, terminated by either party by serving not less than three months' prior written notice or by payment of three months' salary in lieu of such notice. Two directors waived or agreed to waive all of their remuneration and two directors waived or agreed to waive half of their remuneration in 2001 and 2002.

## Notes to the Financial Statements

(Expressed in Hong Kong dollars)

### 8. INDIVIDUALS WITH HIGHEST EMOLUMENTS

Of the five individuals with the highest emoluments, four (2001: two) are directors whose emoluments are disclosed in note 7. The aggregate of the emoluments in respect of the remaining one (2001: three) individual is as follows:

	2002 \$'000	2001 \$'000
Basic salaries, allowances and other benefits	165	206
Discretionary bonuses	14	–
Retirement benefit scheme contributions	–	2
	<b>179</b>	<b>208</b>

The emoluments of the remaining one (2001: three) individual with the highest emoluments are within the following band:

	2002 Number of individuals	2001 Number of individuals
Nil – \$1,000,000	1	3

During the year, no emoluments were paid to the Directors and the five highest paid individuals as an inducements to join or upon joining the Group or as compensation for loss of office.

### 9. PROFIT ATTRIBUTABLE TO SHAREHOLDERS

The consolidated profit attributable to shareholders includes a loss of \$4,785,000 (2001: \$731,000) which has been dealt with in the financial statements of the Company.

### 10. EARNINGS PER SHARE

#### (a) Basic earnings per share

The calculation of basic earnings per share for the year ended 31 December 2002 is based on the profit attributable to shareholders of \$22,979,000 divided by the weighted average number of 814,095,890 shares in issue during the year.

The calculation of basic earnings per share for the year ended 31 December 2001 is based on the profit attributable to shareholders of \$22,403,000 divided by the weighted average number of 515,629,589 shares, prior to the placing but after adjusting the effect of the capitalization issue on 20 December 2001.

# Notes to the Financial Statements

(Expressed in Hong Kong dollars)

## 10. EARNINGS PER SHARE (continued)

### (b) Diluted earnings per share

No diluted earnings per share is shown as the Company had no dilutive potential ordinary shares as at 31 December 2002.

The calculation of diluted earnings per share for the year ended 31 December 2001 is based on the adjusted profit attributable to shareholders of \$22,719,000 and the weighted average number of ordinary shares of 657,972,603 shares after adjusting for the effects of the dilutive potential ordinary shares committed under the convertible loan issued on 8 September 2000 which entitled the noteholders to convert the paid up principal into 30% enlarged issued share capital of the Tat Lung Medical Treatment Technology Limited (“Tat Lung Hong Kong”) upon conversion.

### (c) Reconciliation

	2001
	\$'000
Profit attributable to shareholders	22,403
Interest paid for the convertible loan	316
Adjusted profit attributable to shareholders	22,719
	2001
	Number of shares
Weighted average number of ordinary shares used in calculating basic earnings per share	515,629,589
Deemed issue of ordinary shares	142,343,014
Weighted average number of ordinary shares used in calculating diluted earnings per share	657,972,603



# Notes to the Financial Statements

(Expressed in Hong Kong dollars)

## 11. FIXED ASSETS

### (a) The Group

	Medical equipment \$'000	Office, computer and other equipment \$'000	Motor vehicles \$'000	Total \$'000
<b>Cost:</b>				
At 1 January 2002	27,814	251	–	28,065
Additions	3,487	855	999	5,341
Disposals	(471)	–	–	(471)
Exchange adjustment	(5)	(1)	–	(6)
<b>At 31 December 2002</b>	<b>30,825</b>	<b>1,105</b>	<b>999</b>	<b>32,929</b>
<b>Aggregate depreciation:</b>				
At 1 January 2002	(5,594)	(51)	–	(5,645)
Charged for the year	(4,510)	(75)	(137)	(4,722)
Written back on disposal	45	–	–	45
Exchange adjustment	1	–	–	1
<b>At 31 December 2002</b>	<b>(10,058)</b>	<b>(126)</b>	<b>(137)</b>	<b>(10,321)</b>
<b>Net book value:</b>				
<b>At 31 December 2002</b>	<b>20,767</b>	<b>979</b>	<b>862</b>	<b>22,608</b>
At 31 December 2001	22,220	200	–	22,420

# Notes to the Financial Statements

(Expressed in Hong Kong dollars)

## 11. FIXED ASSETS (continued)

### (b) The Company

	Office, computer and other equipment \$'000	Motor vehicles \$'000	Total \$'000
<b>Cost:</b>			
At 1 January 2002	–	–	–
Additions	70	803	873
<b>At 31 December 2002</b>	<b>70</b>	<b>803</b>	<b>873</b>
<b>Aggregate depreciation:</b>			
At 1 January 2002	–	–	–
Charge for the year	(10)	(134)	(144)
<b>At 31 December 2002</b>	<b>(10)</b>	<b>(134)</b>	<b>(144)</b>
<b>Net book value:</b>			
<b>At 31 December 2002</b>	<b>60</b>	<b>669</b>	<b>729</b>
At 31 December 2001	–	–	–

## 12. CONSTRUCTION IN PROGRESS

	The Group	
	2002 \$'000	2001 \$'000
Balance at 1 January	–	–
Additions	1,547	–
Balance at 31 December	1,547	–

## Notes to the Financial Statements

(Expressed in Hong Kong dollars)

### 13. INVESTMENTS IN SUBSIDIARIES

	The Company	
	2002 \$'000	2001 \$'000
Unlisted shares, cost	14,830	5,465

Details of the subsidiaries at 31 December 2002 are as follows. The class of shares held is ordinary unless otherwise stated.

All of these are controlled subsidiaries as defined under note 2(e) and have been consolidated into the consolidated financial statements.

Name of company	Place of incorporation/ establishment and operation	Percentage of equity			Issued/ registered capital	Principal activities	Note
		Group's effective holding	held by the Company	held by subsidiary			
Future Asia Management Limited	British Virgin Islands ("B.V.I.")	100%	100%	–	US\$20,000	Investment holding	
Tat Lung Hong Kong	Hong Kong	100%	–	100%	\$142,900	Investment holding	
Tat Lung Shenzhen	PRC	100%	–	100%	\$5,000,000	Provision of medical equipment and related services	(i)
China Best	PRC	100%	100%	–	US\$3,000,000	Research and development of medicine and drugs	(ii)
Sino-Innova	PRC	90%	90%	–	US\$2,600,000	Manufacturing and sale of medical equipment	(iii)

# Notes to the Financial Statements

(Expressed in Hong Kong dollars)

## 13. INVESTMENTS IN SUBSIDIARIES (continued)

Notes:

- (i) The subsidiary is a wholly foreign owned enterprise set up to provide medical equipment and related services.
- (ii) The subsidiary is a wholly foreign owned enterprise established in Nanjing, the PRC and set up to establish a research centre for medicine and drugs. During the year, the Company contributed US\$500,000 as the initial capital contribution. JiangSu TianHua Dapeng Certified Public Accountants Co. Ltd. have verified the above capital contribution, and issued the related capital verification report on 30 September 2002.

It commenced operation in September 2002. Pursuant to a research projects acquisition and reorganisation agreement with Miss Guo Ping dated 6 December 2002, the subsidiary will acquire certain medicine research projects after year ended 31 December 2002. Please refer to Note 29(b)(ii) for details.

As at 31 December 2002, the Company's total investment in this subsidiary amounted to US\$500,000. Please refer to Note 29(a) in respect of the capital commitments for the subsidiary.

- (iii) The subsidiary is a sino-foreign enterprise and set up to establish a medical equipment production line in Nanjing, the PRC. During the year, the Company contributed US\$700,000 as the capital contribution. JiangSu XingGuang Certified Public Accountants have verified the above capital contributions, and issued the related capital verification report on 9 December 2002.

Construction of buildings, plant and machinery and equipment of the medical equipment production line has not yet been completed as at 31 December 2002. Accordingly, the subsidiary has not yet commenced production during the year.

As at 31 December 2002, the Company's total investment in this subsidiary amounted to US\$700,000. Please refer to Note 29(a) in respect of the capital commitments for the subsidiary.

## 14. INTEREST IN AN ASSOCIATE

	The Group	
	2002	2001
	\$'000	\$'000
Share of net assets	447	—
	447	—

## Notes to the Financial Statements

(Expressed in Hong Kong dollars)

### 14. INTEREST IN AN ASSOCIATE (continued)

Details of the Group's interest in associate are as follows:

Name of company	Form of business structure	Place of establishment and operation	Percentage of equity			Registered capital	Principal activities
			Group's effective holding	held by the Company	held by subsidiary		
Jiang Xi J&P Biological Products Limited ( <i>Note</i> )	Incorporated	PRC	49%	-	49%	RMB1,000,000	Manufacturing and sale of drugs and medicine

*Note:*

The associate is a sino-foreign enterprise and set up to establish a drugs and medicine production line in Jiang Xi, the PRC. During the year, the Company contributed RMB490,000 as the capital contribution. Yi Chun Zheng Xin Certified Public Accountants have verified the above capital contribution, and issued the related capital verification report on 20 August 2002.

The associate commenced production in August 2002. As at 31 December 2002, the Group's total investment in this associate amounted to RMB490,000.

### 15. NEGATIVE GOODWILL

	The Group	
	2002 \$'000	2001 \$'000
Negative goodwill	(16,029)	(16,029)
Less: Accumulated amortization	7,205	4,323
	<b>(8,824)</b>	(11,706)

The balance represents the negative goodwill arising from the Group's acquisition of the medical equipment business together with the relevant assets from Guangxi Wuzhou Tat Lung Medical Equipment Company Limited ("Wuzhou Tat Lung").

# Notes to the Financial Statements

(Expressed in Hong Kong dollars)

## 16. INVENTORIES

	The Group	
	2002	2001
	\$'000	\$'000
Finished goods	1,200	868
Spare parts	448	–
	<b>1,648</b>	868

All finished goods and spare parts are stated at cost.

## 17. TRADE RECEIVABLES

All of the trade receivables are expected to be recovered within one year.

An ageing analysis of trade receivables (net of provision for bad and doubtful debts) is as follows:

	The Group	
	2002	2001
	\$'000	\$'000
Within 3 months of the date of billing	3,398	2,105

Debts are normally due within 60 days from the date of billing.

## 18. AMOUNTS DUE FROM/(TO) SUBSIDIARIES

Amounts due from/(to) subsidiaries are unsecured, interest free and have no fixed terms of repayment.

## Notes to the Financial Statements

(Expressed in Hong Kong dollars)

### 19. OTHER RECEIVABLES AND PREPAYMENTS

	The Group		The Company	
	2002 \$'000	2001 \$'000	2002 \$'000	2001 \$'000
Proceeds receivable from issuance of Placing Shares	–	13,202	–	13,202
Advances to third party	–	34,462	–	34,462
Other receivables, deposits and prepayments	4,339	3,586	618	–
Acquisition deposit (Note 29(b)(ii))	30,218	–	30,218	–
	<b>34,557</b>	51,250	<b>30,836</b>	47,664

### 20. AMOUNT DUE FROM A RELATED COMPANY

	The Group	
	2002 \$'000	2001 \$'000
Innova Medical Science & Technology Company Limited (“Innova”)	408	–
Maximum amount outstanding during the year	408	–

Innova is the minority shareholder of a subsidiary, Sino-Innova. The amount due from a related company is unsecured, interest free, and has no fixed terms of repayment.

# Notes to the Financial Statements

(Expressed in Hong Kong dollars)

## 21. DEPOSITS WITH BANKS

	The Group	
	2002 \$'000	2001 \$'000
Deposits with banks	93,488	28,286
<i>Less:</i> Deposits with banks with an initial term of less than three months ( <i>Note 22</i> )	–	(11,314)
	<b>93,488</b>	16,972

All deposits with banks are denominated in Renminbi (“RMB”) and kept in the PRC.

The conversion of the RMB balances into foreign currencies and the transfer of these balances out of the PRC are subject to the rules and regulations of foreign exchange control promulgated by the PRC government.

## 22. CASH AND CASH EQUIVALENTS

	The Group		The Company	
	2002 \$'000	2001 \$'000	2002 \$'000	2001 \$'000
Cash at bank and in hand	13,730	15,879	8,657	2,729
<i>Add:</i> Deposits with banks with an initial term of less than three months ( <i>Note 21</i> )	–	11,314	–	–
Cash and cash equivalents	<b>13,730</b>	27,193	<b>8,657</b>	2,729



## Notes to the Financial Statements

(Expressed in Hong Kong dollars)

### 23. TRADE AND OTHER PAYABLES

	The Group		The Company	
	2002 \$'000	2001 \$'000	2002 \$'000	2001 \$'000
Trade payables	3,198	1,279	–	–
Other payables and accrued liabilities	12,588	8,715	2,044	2,665
	15,786	9,994	2,044	2,665

All of the trade and other payables are expected to be settled within one year.

An ageing analysis of trade payables is as follows:

	The Group	
	2002 \$'000	2001 \$'000
Due within 3 months or on demand	3,198	1,279

### 24. AMOUNT DUE TO A RELATED COMPANY

	The Group	
	2002 \$'000	2001 \$'000
Everblooming Enterprises Company (“Everblooming”)	897	897
	897	897

The amount due to a related company is unsecured, interest free, and has no fixed terms of repayment.

### 25. AMOUNT DUE TO A DIRECTOR

The amount is unsecured, interest free and has no fixed terms of repayment.

# Notes to the Financial Statements

(Expressed in Hong Kong dollars)

## 26. SHARE CAPITAL

Note	2002		2001	
	No of shares '000	Amount \$'000	No of shares '000	Amount \$'000
<b>Authorized:</b>				
Ordinary shares of \$0.01 each	2,000,000	20,000	2,000,000	20,000
<b>Issued and fully paid:</b>				
At 1 January	800,000	8,000	–	–
Shares issued under the reorganization	–	–	656,000	6,560
Shares issued under initial public offering	–	–	144,000	1,440
Shares issued under placement of shares (i)	35,000	350	–	–
At 31 December	835,000	8,350	800,000	8,000

Note:

- (i) On 7 August 2002, 35,000,000 ordinary shares of \$0.01 each were issued at a value of \$0.57 per share (the "Placement of shares"). As a result of the Placement of shares, the Group received approximately \$19,259,000 net of related expenses from the issue. The net consideration of \$350,000 was credited to share capital and the balance of \$18,909,000 was credited to the share premium account.

Further details of the Placement of shares were published in the announcements of "Discloseable Transaction-Placing of existing shares and subscription of new shares" and "Completion of Placing of existing shares and subscription of new shares" dated 24 July 2002 and 1 August 2002 respectively.

# Notes to the Financial Statements

(Expressed in Hong Kong dollars)

## 27. RESERVES

### (a) The Group

	General reserve \$'000	Share premium \$'000	Contributed surplus \$'000	Retained profits \$'000	Exchange reserves \$'000	Total \$'000
At 1 January 2001	564	-	-	4,270	7	4,841
Premium on the issuance of shares	-	70,560	-	-	-	70,560
Share issue expenses	-	(12,376)	-	-	-	(12,376)
Capitalization issue of shares	-	(6,360)	-	-	-	(6,360)
Arising on the acquisition of a subsidiary under the reorganization	-	-	5,265	-	-	5,265
Profit for the year	-	-	-	22,403	-	22,403
Appropriations to general reserve	2,390	-	-	(2,390)	-	-
Exchange difference	-	-	-	-	10	10
At 31 December 2001	2,954	51,824	5,265	24,283	17	84,343
At 1 January 2002	2,954	51,824	5,265	24,283	17	84,343
Premium on the issuance of shares	-	19,600	-	-	-	19,600
Share issue expenses	-	(691)	-	-	-	(691)
Profit for the year	-	-	-	22,979	-	22,979
Appropriations to general reserve	2,829	-	-	(2,829)	-	-
Exchange difference	-	-	-	-	(29)	(29)
At 31 December 2002	5,783	70,733	5,265	44,433	(12)	126,202

# Notes to the Financial Statements

(Expressed in Hong Kong dollars)

## 27. RESERVES (continued)

### (b) The Company

	Share premium \$'000	Contributed surplus \$'000	Accumulated losses \$'000	Total \$'000
At 1 January 2001	–	–	–	–
Premium on the issuance of shares	70,560	–	–	70,560
Share issue expenses	(12,376)	–	–	(12,376)
Capitalization issue of shares	(6,360)	–	–	(6,360)
Arising on the acquisition of a subsidiary under the reorganization	–	5,265	–	5,265
Loss for the year	–	–	(731)	(731)
At 31 December 2001	51,824	5,265	(731)	56,358
At 1 January 2002	51,824	5,265	(731)	56,358
Premium on the issuance of shares	19,600	–	–	19,600
Share issue expenses	(691)	–	–	(691)
Loss for the year	–	–	(4,785)	(4,785)
At 31 December 2002	70,733	5,265	(5,516)	70,482

- (c) According to the relevant rules and regulations in the PRC, Tat Lung Shenzhen is required to appropriate 10% of after-tax profit (after offsetting prior year losses), based on the PRC statutory financial statements prepared in accordance with the relevant accounting principles and financial regulations applicable to foreign investment enterprises in the PRC, to a general reserve fund until the balance of the fund reaches 50% of the Tat Lung Shenzhen's registered capital. Thereafter, any further appropriation can be made at the directors' discretion. The general reserve fund can be utilized to offset prior year losses, or be utilized for issuance of bonus shares on condition that the general reserve fund shall be maintained at a minimum of 25% of the registered capital after such issuance.

According to the relevant rules and regulations in the PRC, Tat Lung Shenzhen may also appropriate a portion of its after-tax profit (after offsetting prior year losses), based on Tat Lung Shenzhen's PRC statutory financial statements, to an enterprises expansion fund and a staff and worker's bonus and welfare fund at the directors' discretion. No such appropriations have been made during the relevant year.

## Notes to the Financial Statements

(Expressed in Hong Kong dollars)

### 27. RESERVES (continued)

- (d) The application of the share premium account is governed by Bye-Law 140(A) of the Company's Bye-Laws and the Companies Act 1981 of Bermuda ("Companies Act").
- (e) Pursuant to a group reorganization in 2001, the Company became the holding company of the Group. The excess of the consolidated net assets represented by the shares acquired over the nominal value of the shares issued by the Company in exchange under the Reorganization in 2001 was transferred to contributed surplus. Contributed surplus is available for distribution to shareholders subject to the provisions of section 54 of the Companies Act.
- (f) The exchange reserves have been set up and will be dealt with in accordance with the accounting policies adopted for foreign currency translation.
- (g) Included in the retained profits is an amount of \$15,000 (2001: Nil), being the accumulated losses attributable to associates.
- (h) At 31 December 2001 and 2002, the Company had no reserve, other than contributed surplus, available for distribution to shareholders.

# Notes to the Financial Statements

(Expressed in Hong Kong dollars)

## 28. NOTES TO THE CONSOLIDATED CASH FLOW STATEMENT

### (a) Major non-cash transactions

- (i) Part of the outstanding balance due from related company. Wuzhou Tat Lung, at 30 June 2001 of \$1,885,000 was assigned to Everblooming which is a related company and supplier of the Group, to settle an equivalent amount due to Everblooming.
- (ii) On 21 September 2001, an aggregate 4,290 shares of \$1 each of Tat Lung Hong Kong were allotted, issued and credited as fully paid to Mr. Li Wo Hing and his designated person upon the conversion of the convertible loan.

### (b) Acquisition of business

	2001
	\$'000
<hr/>	
Net assets acquired:	
Fixed assets	20,743
Negative goodwill	(16,029)
	<hr/>
	4,714
<hr/>	
Satisfied by:	
Cash	4,714
	<hr/>

On 30 June 2000, the Group acquired Wuzhou Tat Lung's provision of medical equipment business in the PRC together with the relevant assets at a consideration of \$4,714,000. The amount was paid during the year ended 31 December 2001.

## Notes to the Financial Statements

(Expressed in Hong Kong dollars)

### 29. COMMITMENTS

#### (a) Capital commitments

Capital commitments in respect of capital contribution to the subsidiaries, land, buildings, and plant and machineries outstanding at 31 December 2002 not provided for in the financial statements were as follows:

##### (i) Contracted for:

	The Group		The Company	
	2002 \$'000	2001 \$'000	2002 \$'000	2001 \$'000
Capital contributions to the subsidiaries	–	–	32,292	–
Land, buildings and plant and machineries	5,415	–	–	–
	5,415	–	32,292	–

##### (ii) Authorized but not contracted for:

	The Group		The Company	
	2002 \$'000	2001 \$'000	2002 \$'000	2001 \$'000
Plant and machineries and other fixed assets	–	4,800	–	–
	–	4,800	–	–

# Notes to the Financial Statements

(Expressed in Hong Kong dollars)

## 29. COMMITMENTS (continued)

### (b) Other commitment

- (i) During 2002, the Company entered into a cooperation memorandum with Fudan University to donate RMB10,000,000 from 2002 to 2008 for the establishment of the “复旦大學藥學院神州佳美新葯研究開發基金”. The remaining amount of RMB9,000,000 is payable as follows:

	RMB'000
2003	1,000
2004	1,500
2005	1,500
2006	1,500
2007	1,500
2008	2,000
	9,000

- (ii) On 6 December 2002, the Company entered into a research projects acquisition and reorganization agreement (“the agreement”) with Miss Guo Ping for the acquisition of 75% interest in 16 medicine research projects for a consideration of US\$8,000,000.

The acquisition will be completed within six months from the date of agreement.

Pursuant to the agreement, the Company had paid a deposit amounting to \$30,218,000 as at 31 December 2002. (Note 19)

Details of the said acquisition and reorganization were set out in the announcement of “Discloseable Transaction - acquisition of the medicine research projects” dated 6 December 2002.



# Notes to the Financial Statements

(Expressed in Hong Kong dollars)

## 29. COMMITMENTS (continued)

### (c) Operating lease commitments

At 31 December 2002, the total future minimum lease payments under non-cancellable operating leases in respect of land and buildings are payable as follows:

	The Group	
	2002 \$'000	2001 \$'000
Within 1 year	112	493
After 1 year but within 5 years	–	65
	<b>112</b>	<b>558</b>

The Group leases a number of properties under operating leases. The leases typically run for an initial period of one year, with an option to renew the lease when all terms are renegotiated. The leases do not include contingent rentals.

## 30. RETIREMENT BENEFIT SCHEMES

### Hong Kong

Since 1 December 2000, the Hong Kong subsidiary is required to join the Mandatory Provident Fund (the “MPF”), managed by an independent approved MPF trustee, under the requirements of the Mandatory Provident Fund Schemes Ordinance.

A new Mandatory Provident Fund scheme (the “MPF Scheme”) has been set up by the Group for this purpose and employer contributions are made under the MPF Scheme. Contributions are made based on a percentage of the employees’ basic salaries and are charged to the income statement as they became payable in accordance with the rules of the MPF Scheme. The Group’s employer contributions vest fully with the employees when contributed to the scheme in accordance with the rules of the MPF Scheme. No forfeited contributions were utilized or available for the year.

# Notes to the Financial Statements

(Expressed in Hong Kong dollars)

## 30. RETIREMENT BENEFIT SCHEMES (continued)

### PRC, other than Hong Kong

The PRC subsidiaries of the Group participate in a mandatory central pension scheme organized by the PRC government for certain of its employees, the assets of which are held separately from those of the Group. Contributions made are based on a percentage of the eligible employees' salaries and are charged to the income statement as they became payable, in accordance with the rules of the scheme. The employer contributions vest fully once they are made.

Under the above schemes, retirement benefits of existing and retired employees are payable by the relevant scheme administrators and the Group has no further obligations beyond the annual contributions.

The aggregate amount of employer contributions by the Group in respect of retirement benefit schemes dealt with in the income statement of the Group is disclosed in note 5(b) to the financial statements.

## 31. SHARE OPTION SCHEME

On 14 December 2001, the Company has conditionally adopted a share option scheme pursuant to which any employees and directors of the Company and its subsidiaries may be granted options to subscribe for the shares of the Company.

During the year, no options were granted under the share option scheme.

# Notes to the Financial Statements

(Expressed in Hong Kong dollars)

## 32. RELATED PARTY TRANSACTIONS

During the year, the Group had the following transactions with related parties:

	Note	2002 \$'000	2001 \$'000
Everblooming	(i)		
Purchase of medical accessories		–	3,970
Purchase of medical equipment		–	6,936
Li Wo Hing			
Interest expense on convertible loan	(ii)	–	316
Advances to Innova	(iii)	408	–
Advances from a director	(iv)	888	672

Notes:

- (i) Everblooming, a sole proprietorship registered in the United States of America and wholly-owned by Dr Li Nga Kuk, James who is a shareholder and director of the Company and director of Tat Lung Hong Kong, supplies Tat Lung Shenzhen with medical equipment and accessories at cost.

Tat Lung Shenzhen ordered certain medical equipment totalling \$2,356,000 from Everblooming in June 2001. Downpayments totalling \$1,459,000 were paid pursuant to the relevant sales and purchases agreement, the remaining balance of \$897,000 was included as amount due to related company at 31 December 2001 and 2002.

- (ii) On 8 September 2000, Mr Li Wo Hing entered into an agreement with Dr Li Nga Kuk, James and Mr Ng Kwai Sang whereby Mr Li Wo Hing provided a loan of \$5,455,000 to Tat Lung Hong Kong, which was convertible into new shares of Tat Lung Hong Kong representing 30% of the enlarged issued share capital of Tat Lung Hong Kong upon conversion. Mr Li Wo Hing was appointed director of the Tat Lung Shenzhen on 30 December 2000. The convertible loan was unsecured and interest bearing at a fixed rate of 8% per annum.

The interest payable to Mr Li Wo Hing included in trade and other payables as at 31 December 2002 amounted to \$Nil (2001: \$453,000).

On 21 September 2001, the right attached to the convertible loan was exercised in full by Mr Li Wo Hing and accordingly, in accordance with the terms and conditions of the convertible loan, 4,290 shares of \$1 each of Tat Lung Hong Kong were allotted to Mr Li Wo Hing and his designated person in full settlement of the loan liability.

- (iii) During the year ended 31 December 2002, the Group advanced to Innova, a minority shareholder, an amount of \$408,000 (2001: Nil). All advances are interest free, unsecured and have no fixed repayment terms.

- (iv) During the year ended 31 December 2002, the Group borrowed from a director an amount of \$888,000 (2001: \$672,000). All borrowings are interest free, unsecured and have no fixed repayment terms.

# Notes to the Financial Statements

*(Expressed in Hong Kong dollars)*

## **32. RELATED PARTY TRANSACTIONS (continued)**

The Directors of the Company are of the opinion that the above transactions with the related parties were conducted on normal commercial terms and in the ordinary course of business.

Apart from the above there were no other material related party transactions entered into by the Group during the year.

## **33. COMPARATIVE FIGURES**

The presentation and classification of items in the consolidated cash flow statement have been changed due to the adoption of the requirements of SSAP15 (revised 2001) Cash flow statements. As a result, cash flow items from taxation, returns on investments and servicing of finance have been classified into operating, investing and financing activities respectively and a detailed breakdown of cash flows from operating activities has been included on the face of the consolidated cash flow statement. Comparative figures have been reclassified to conform with the current year's presentation.

## Three Years' Summary

(Expressed in Hong Kong dollars)

	2000	2001	2002
	\$'000	\$'000	\$'000
<b>Results</b>			
Turnover	11,017	38,523	<b>49,850</b>
Profit from operations	5,966	26,936	<b>27,987</b>
Finance costs	(137)	(316)	–
Share of loss of associate	–	–	<b>(15)</b>
Profit from ordinary activities			
before taxation	5,829	26,620	<b>27,972</b>
Taxation	(995)	(4,217)	<b>(4,993)</b>
Profit attributable to shareholders	4,834	22,403	<b>22,979</b>
<b>Assets and liabilities</b>			
Fixed Assets	19,053	22,420	<b>22,608</b>
Construction in progress	–	–	<b>1,547</b>
Negative goodwill	(14,588)	(11,706)	<b>(8,824)</b>
Interest in an associate	–	–	<b>447</b>
Net current assets	5,841	81,629	<b>118,774</b>
Non-current liabilities	(5,455)	–	–
NET ASSETS	4,851	92,343	<b>134,552</b>
Share capital	10	8,000	<b>8,350</b>
Reserves	4,841	84,343	<b>126,202</b>
	4,851	92,343	<b>134,552</b>
<b>Earnings per share (in Hong Kong cents)</b>			
Basic	1.05	4.34	<b>2.82</b>
Diluted	0.95	3.45	<b>N/A</b>