

CHINA MEDICAL SCIENCE LIMITED

中華藥業有限公司*

(Incorporated in the Cayman Islands with limited liability)

SECOND QUARTERLY REPORT

2004

** For identification purposes only*

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 of the Stock Exchange 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 Stock Exchange. Listed companies are not generally required to issue paid announcements in gazetted newspaper. 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.

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

HIGHLIGHTS

- Turnover of the Group for the six months ended 31 January 2004 amounted to approximately HK\$95,676,000.
- Loss attributable to shareholders for the six months ended 31 January 2004 amounted to approximately HK\$6,232,000.
- Basic loss per share amounted to approximately 1.25 cents for the six months ended 31 January 2004.
- The Directors do not recommend the payment of any interim dividend for the six months ended 31 January 2004.

RESULTS

The board of directors (the “Board”) of China Medical Science Limited (the “Company”) is pleased to announce that the unaudited consolidated results of the Company and its subsidiaries (collectively, the “Group”) for the three months and the six months ended 31 January 2004, together with the comparative unaudited figures for the corresponding periods of the previous financial year are as follows:

Consolidated Income Statement – Unaudited

| | Note | For the three months ended 31 January | | For the six months ended 31 January | |
|--|------|--|------------------|--|------------------|
| | | 2004 HK\$'000 | 2003 HK\$'000 | 2004 HK\$'000 | 2003 HK\$'000 |
| Turnover | 2 | 43,400 | 28,183 | 95,676 | 62,609 |
| Cost of sales | | (35,487) | (19,204) | (76,675) | (42,655) |
| Gross profit | | 7,913 | 8,979 | 19,001 | 19,954 |
| Other revenue & gains | 2 | 340 | 627 | 1,046 | 1,268 |
| Selling and distribution costs | | (2,855) | (1,374) | (6,348) | (1,887) |
| General and administrative expenses | | (4,021) | (2,636) | (8,241) | (5,930) |
| Other operating expenses | | (2,207) | (1,381) | (3,661) | (2,697) |
| PROFIT/(LOSS) FROM OPERATING ACTIVITIES | 4 | (830) | 4,215 | 1,797 | 10,708 |
| Finance costs | | (4,128) | (2,096) | (8,150) | (4,812) |
| Share of profit/(loss) of an associate | | 246 | (103) | 592 | (201) |
| (LOSS)/PROFIT BEFORE TAX | | (4,712) | 2,016 | (5,761) | 5,695 |
| Tax | 5 | - | (123) | - | (415) |
| (LOSS)/PROFIT BEFORE MINORITY INTERESTS | | (4,712) | 1,893 | (5,761) | 5,280 |
| Minority interests | | 136 | (192) | (471) | (538) |
| NET (LOSS)/PROFIT FROM ORDINARY ACTIVITIES ATTRIBUTABLE TO SHAREHOLDERS | | (4,576) | 1,701 | (6,232) | 4,742 |
| Interim Dividend | | - | - | - | - |
| (LOSS)/EARNINGS PER SHARE | 6 | (0.92 cents) | 0.34 cents | (1.25 cents) | 0.95 cents |
| - Basic | | (0.92 cents) | 0.34 cents | (1.25 cents) | 0.95 cents |
| - Diluted | | N/A | 0.34 cents | N/A | 0.93 cents |

Condensed Consolidated Balance Sheet

| | | As at 31 January 2004 HK\$'000 (Unaudited) | As at 31 July 2003 HK\$'000 (Restated) |
|--|------|--|--|
| | Note | | |
| NON-CURRENT ASSETS | | | |
| Fixed assets | 7 | 204,759 | 204,339 |
| Intangible assets | | 14,397 | 9,485 |
| Goodwill: | | | |
| Goodwill | | 17,254 | 17,731 |
| Negative goodwill | | (5,969) | (6,134) |
| Interest in an associate | | 8,726 | 8,134 |
| Long term investments | | 4,421 | 4,420 |
| Long term prepayment | | 2,583 | 5,405 |
| | | <u>246,171</u> | <u>243,380</u> |
| CURRENT ASSETS | | | |
| Inventories | | 23,351 | 28,535 |
| Trade receivables | 8 | 185,556 | 178,157 |
| Other receivables | 8 | 25,607 | 30,831 |
| Pledged deposits | | 53,909 | 63,512 |
| Cash and cash equivalents | | 55,738 | 45,754 |
| | | <u>344,161</u> | <u>346,789</u> |
| CURRENT LIABILITIES | | | |
| Trade payables | 9 | 69,146 | 66,202 |
| Notes payable | 9 | 115,229 | 103,695 |
| Tax payable | | 1,631 | 1,631 |
| Current portion of finance lease payment | | 847 | – |
| Other payables and accruals | 9 | 56,245 | 57,783 |
| Interest-bearing bank and other borrowings | | 159,572 | 196,394 |
| Due to a director | | 4,948 | 1,586 |
| | | <u>407,618</u> | <u>427,291</u> |
| NET CURRENT LIABILITIES | | <u>63,457</u> | <u>80,502</u> |
| TOTAL ASSETS LESS CURRENT LIABILITIES | | <u>182,714</u> | <u>162,878</u> |
| NON-CURRENT LIABILITIES | | | |
| Interest-bearing bank and other loans | | 47,389 | 26,741 |
| Non-current portion of finance lease payment | | 4,164 | – |
| Deferred taxation | | 358 | 367 |
| | | <u>130,803</u> | <u>135,770</u> |
| Minority interests | | 17,299 | 16,034 |
| | | <u>113,504</u> | <u>119,736</u> |
| CAPITAL AND RESERVES | | | |
| Issued capital | 10 | 25,000 | 25,000 |
| Reserves | | 88,504 | 94,736 |
| | | <u>113,504</u> | <u>119,736</u> |

Condensed Consolidated Cash Flow Statement – Unaudited

| | For the six months ended 31 January 2004 HK\$'000 | For the six months ended 31 January 2003 HK\$'000 <i>(Restated)</i> |
|--|--|---|
| NET CASH INFLOW FROM OPERATING ACTIVITIES | 27,190 | 18,263 |
| NET CASH OUTFLOW FROM INVESTING ACTIVITIES | (6,177) | (4,700) |
| NET CASH OUTFLOW FROM FINANCING ACTIVITIES | (11,029) | (113) |
| NET INCREASE IN CASH AND CASH EQUIVALENTS | 9,984 | 13,450 |
| CASH AND CASH EQUIVALENTS AT BEGINNING OF THE PERIOD | 45,754 | 31,387 |
| CASH AND CASH EQUIVALENTS AT END OF THE PERIOD | <u>55,738</u> | <u>44,837</u> |
| ANALYSIS OF BALANCES OF CASH AND CASH EQUIVALENTS | | |
| Non-pledged cash and bank balances | 19,319 | 2,596 |
| Non-pledged time deposits with original maturity of less than three months when acquired | 36,419 | 42,241 |
| | <u>55,738</u> | <u>44,837</u> |

Condensed Consolidated Statement of Change in Equity – Unaudited

| | Issued share capital <i>HK\$'000</i> | Share premium <i>HK\$'000</i> | Capital reserve <i>HK\$'000</i> | Exchange fluctuation reserve <i>HK\$'000</i> | Retained profits <i>HK\$'000</i> | Total <i>HK\$'000</i> |
|---------------------------|---|-------------------------------------|---------------------------------------|---|--|--------------------------|
| At 1 August 2002 | 25,000 | 17,992 | 27,104 | 25 | 50,267 | 120,388 |
| Net profit for the period | – | – | – | – | 4,742 | 4,742 |
| | <u>25,000</u> | <u>17,992</u> | <u>27,104</u> | <u>25</u> | <u>55,009</u> | <u>125,130</u> |
| At 31 January 2003 | 25,000 | 17,992 | 27,104 | 25 | 49,615 | 119,736 |
| Net loss for the period | – | – | – | – | (6,232) | (6,232) |
| | <u>25,000</u> | <u>17,992</u> | <u>27,104</u> | <u>25</u> | <u>43,383</u> | <u>113,504</u> |
| At 31 January 2004 | 25,000 | 17,992 | 27,104 | 25 | 43,383 | 113,504 |

Notes:

1. Group reorganisation and basis of presentation

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

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

The principal accounting policies adopted in preparing the unaudited consolidated results are consistent with those used in the annual financial statements for the year ended 31 July 2003 of the Group, except that the Group has adopted the SSAP 12 (revised) "Income Taxes" issued by the Hong Kong Society of Accountants which became effective on 1 January 2003. The adoption of SSAP 12 (revised) does not have any significant effect on the Group's unaudited consolidated results.

2. Turnover

Turnover represents the net invoiced value of goods sold, after allowances for returns and trade discounts.

An analysis of turnover, other revenue and gains is as follows:

| | For the three months ended 31 January 2004 | | For the six months ended 31 January 2004 | |
|--------------------------------|---|---------------|---|---------------|
| | HK\$'000 | HK\$'000 | HK\$'000 | HK\$'000 |
| Turnover | | | | |
| Sale of human drugs | 35,044 | 14,816 | 74,891 | 29,634 |
| Sale of veterinary drugs | 5,075 | 6,405 | 11,015 | 13,883 |
| Sale of packaging materials | 3,281 | 6,962 | 9,770 | 19,092 |
| | <u>43,400</u> | <u>28,183</u> | <u>95,676</u> | <u>62,609</u> |
| Other revenue and gains | | | | |
| Interest income | 26 | 449 | 532 | 913 |
| Sundry income | 140 | 4 | 165 | 8 |
| Negative goodwill recognized | 174 | 174 | 349 | 347 |
| | <u>340</u> | <u>627</u> | <u>1,046</u> | <u>1,268</u> |

3. Segment information

An analysis of the Group's turnover and contribution to operating results by business segments is as follows:

| | Human drugs | | Veterinary drugs | | Packaging materials | | Corporate | | Eliminations | | Consolidated | |
|---|---------------|---------------|------------------|---------------|---------------------|---------------|--------------|--------------|----------------|----------------|----------------|---------------|
| | 2004 | 2003 | 2004 | 2003 | 2004 | 2003 | 2004 | 2003 | 2004 | 2003 | 2004 | 2003 |
| | HK\$000 | HK\$000 | HK\$000 | HK\$000 | HK\$000 | HK\$000 | HK\$000 | HK\$000 | HK\$000 | HK\$000 | HK\$000 | HK\$000 |
| Segment revenue: | | | | | | | | | | | | |
| Sales to external customers | 74,891 | 29,634 | 11,015 | 13,883 | 9,770 | 19,092 | - | - | - | - | 95,676 | 62,609 |
| Intersegment sales | 3,668 | - | - | - | 637 | 555 | - | - | (4,305) | (555) | - | - |
| Other revenue | 153 | 3 | 12 | - | - | 4 | 1,140 | 1,252 | (791) | (904) | 514 | 355 |
| Total | 78,712 | 29,637 | 11,027 | 13,883 | 10,407 | 19,651 | 1,140 | 1,252 | (5,096) | (1,459) | 96,190 | 62,964 |
| Segment results | 4,015 | 4,293 | (236) | 2,957 | (686) | 3,414 | (1,828) | (869) | - | - | 1,265 | 9,795 |
| Interest Income | | | | | | | | | | | 532 | 913 |
| Profit from operating activities | | | | | | | | | | | 1,797 | 10,708 |
| Finance costs | | | | | | | | | | | (8,150) | (4,812) |
| Share of profit/(loss) of an associate | 592 | (201) | - | - | - | - | - | - | - | - | 592 | (201) |
| (Loss)/profit before tax | | | | | | | | | | | (5,761) | 5,695 |
| Tax | - | - | - | (415) | - | - | - | - | - | - | - | (415) |
| (Loss)/profit before minority interests | | | | | | | | | | | (5,761) | 5,280 |
| Minority interests | | | | | | | | | | | (471) | (538) |
| Net (loss)/profit from ordinary activities attributable to shareholders | | | | | | | | | | | <u>(6,232)</u> | <u>4,742</u> |

4. Profit/(Loss) from operating activities

The Group's profit/(loss) from operating activities is arrived at after charging/(crediting):

| | For the three months ended 31 January | | For the six months ended 31 January | |
|-----------------------------------|---------------------------------------|----------|-------------------------------------|----------|
| | 2004 | 2003 | 2004 | 2003 |
| | HK\$'000 | HK\$'000 | HK\$'000 | HK\$'000 |
| Cost of inventories sold | 35,487 | 19,204 | 76,675 | 42,655 |
| Depreciation of fixed assets | 3,978 | 1,611 | 8,120 | 3,774 |
| Amortisation of intangible assets | 1,046 | 965 | 2,012 | 1,930 |
| Interest income | (26) | (449) | (532) | (913) |

5. Tax

No provision for Hong Kong profits tax has been made, as the Group had no assessable profits arising in Hong Kong for the six months ended 31 January 2004 (2003: Nil). Taxes on profits assessable elsewhere have been calculated at the rates of tax prevailing in the countries in which the Group operates, based on existing legislation, interpretations and practices in respect thereof.

The Group did not have any significant unprovided deferred tax liabilities for the six months ended 31 January 2004 (2003: Nil).

6. (Loss)/earnings per share

The calculation of the basic (loss)/earnings per share for the three months and six months ended 31 January 2004 was based on the unaudited net (loss)/profit attributable to shareholders of approximately HK\$(4,576,000) and approximately HK\$(6,232,000) respectively (three months and six months ended 31 January 2003: approximately HK\$1,701,000 and approximately HK\$4,742,000 respectively) and the weighted average number of 500,000,000 for the three months and six months ended 31 January 2004 (three months and six months ended 31 January 2003: 500,000,000) ordinary shares in issue during the period.

The diluted loss per share amount for the three months and six months ended 31 January 2004 has not been disclosed, as the convertible note outstanding during the period had an anti-dilutive effect on the basic loss per share for the period.

The calculation of diluted earnings per share for the three months and six months ended 31 January 2003 was based on the unaudited net profit attributable to shareholders of approximately HK\$1,871,000 and HK\$5,081,000 respectively. The weighted average number of ordinary shares used in the calculation was the 500,000,000 ordinary shares in issue during the period, as used in the basic earnings per share calculation, and the weighted average of 48,619,564 ordinary shares assumed to have been issued at no consideration on the deemed exercise of all convertible note during that period.

7. Fixed Assets

During the period from 1 August 2003 to 31 January 2004, the Group had additions to buildings, plant and equipment and motor vehicles in the amount of approximately HK\$10,758,000.

8. Trade and other receivables

| | 31 January 2004 HK\$'000 (Unaudited) | 31 July 2003 HK\$'000 (Audited) |
|-------------------|---|--|
| Trade receivables | 185,556 | 178,157 |
| Other receivables | 25,607 | 30,831 |
| | <u>211,163</u> | <u>208,988</u> |

The Group's trading terms with its customers are mainly on credit, except for new customers, where payment in advance is normally required. The credit period is generally for a period of three months for major customers. Each customer has a maximum credit limit. The Group seeks to maintain strict control over its outstanding receivables. Overdue balances are reviewed regularly by management.

The ageing analysis for trade receivables, net of provision for bad debt, is as follows:

| | 31 January 2004 HK\$'000 (Unaudited) | 31 July 2003 HK\$'000 (Audited) |
|-----------------|---|--|
| Within 3 months | 107,400 | 112,334 |
| 3 to 6 months | 40,376 | 29,933 |
| 6 to 12 months | 10,528 | 32,259 |
| Over 1 year | 27,252 | 3,631 |
| | <u>185,556</u> | <u>178,157</u> |

9. Trade payables, notes payable and accruals

| | 31 January 2004 HK\$'000 (Unaudited) | 31 July 2003 HK\$'000 (Audited) |
|-----------------------------|---|--|
| Trade payables | 69,146 | 66,202 |
| Notes payable | 115,229 | 103,695 |
| Other payables and accruals | 56,245 | 57,783 |
| | <u>240,620</u> | <u>227,680</u> |

An aged analysis of the trade payables based on payment due date, is as follows:

| | 31 January 2004 HK\$'000 (Unaudited) | 31 July 2003 HK\$'000 (Audited) |
|-----------------|---|--|
| Within 3 months | 41,321 | 32,655 |
| 3 to 6 months | 6,991 | 15,138 |
| 6 to 12 months | 7,650 | 8,328 |
| Over 1 year | 13,184 | 10,081 |
| | <u>69,146</u> | <u>66,202</u> |

10. Share capital

| | No. of shares | | Nominal value | |
|------------------------|------------------|------------------|---------------|---------------|
| | At 31 January | At 31 July | At 31 January | At 31 July |
| | 2004 | 2003 | 2004 | 2003 |
| | '000 | '000 | HK\$'000 | HK\$'000 |
| Authorised: | | | | |
| Ordinary share of | | | | |
| HK\$0.05 each | <u>1,000,000</u> | <u>1,000,000</u> | <u>50,000</u> | <u>50,000</u> |
| Issued and fully paid: | | | | |
| Ordinary share of | | | | |
| HK\$0.05 each | <u>500,000</u> | <u>500,000</u> | <u>25,000</u> | <u>25,000</u> |

DIVIDEND

The Directors do not recommend the payment of any interim dividend for the six months ended 31 January 2004. (2003: Nil)

BUSINESS REVIEW AND OUTLOOK

FINANCIAL REVIEW

For the six months ended 31 January 2004, the Group recorded an unaudited consolidated turnover of approximately HK\$95,676,000 (2003: approximately HK\$62,609,000), representing a substantial increase of approximately 52.8 per cent, as compared with that of the corresponding period in 2003. The group's unaudited consolidated (loss)/profit attributable to shareholders for the period was approximately HK\$(6,232,000) (2003: approximately HK\$4,742,000). This is mainly due to intensified competition in the infusion medicine and packaging material markets, with product price declining on one hand. This caused a decrease in sale of infusion medicine and packaging materials of approximately 45.6% and approximately 48.8% respectively as compared with the corresponding period in the previous year. On the other hand, the regulatory changes introduced by the Ministry of Agriculture caused the return of veterinary drugs for repackaging, which resulted in the overall production schedule of veterinary drugs falling behind the original plan and also a decrease of turnover thereof.

Segment information

For the period under review, the Group is principally engaged in three business segments, which included human drugs, veterinary drugs and packaging materials for infusion medicine. All the activities of the business segments were mainly based in the PRC. The Group presented its segment information based on nature of their operations and the products they provided.

Liquidity, financial resources and capital structure

The Group financed its operation through internally generated cashflows and banking facilities provided by its principal banks in the PRC. In view of the Group's current liquidity position, the Directors expect that the Group will have sufficient funds to meet the need for operation and investment in future.

As at 31 January 2004, the aggregate borrowings were approximately HK\$206,961,000 (31 July 2003: approximately HK\$223,135,000) of which approximately HK\$107,020,000 (31 July 2003: approximately HK\$111,265,000) were partially secured by pledged bank deposits or by assets of certain subsidiaries. As at 31 January 2004, the amount of banking facilities available

and utilized was approximately HK\$285,627,000 (31 July 2003: approximately \$290,122,000). Except for the 3% Convertible Note, the Group's bank and other loans bear interest at the prevailing market rate.

The Group continues to adhere to prudent treasury policy with all bank deposits in either Hong Kong Dollars, or in the local currencies of the operating subsidiaries, keeping a minimum exposure to foreign exchange risks.

Gearing ratio

As at 31 January 2004, the gearing ratio (total borrowing, including notes payables, less cash and cash equivalents and pledged bank deposits to total assets) was approximately 36% (31 July 2003: approximately 36.9%)

Foreign exchange exposure

During the six months ended 31 January 2004 and 2003, the Group mainly earns revenue and incurs cost in Renminbi. The Directors consider that the impact of foreign exchange exposure of the Group is minimal and therefore, no hedging against foreign currency exposure is considered necessary.

Charges on group asset

As at 31 January 2004, certain of the Group's leasehold land and buildings situated in the PRC, plant and machinery with net book values of approximately HK\$65,614,000 (31 July 2003: approximately HK\$68,337,000), and HK\$32,417,000 (31 July 2003: approximately HK\$35,232,000) respectively and bank and time deposits of approximately HK\$53,909,000 (31 July 2003: approximately HK\$63,512,000) were pledged to secure general banking facilities granted to the Group.

Contingent liabilities

As at 31 January 2004, the Group did not have any significant contingent liabilities. (31 July 2003: nil)

Capital commitments and significant investment

At 31 January 2004, the Group had outstanding capital commitment of approximately HK\$2,230,000 (31 July 2003: approximately HK\$4,943,000) and the Group did not have any significant investments.

Future plan for investment

Except as disclosed in the financial statements, as at 31 January 2004, the Group had no future plan for material investment and capital assets.

Material acquisitions/disposals

During the period ended 31 January 2004, the group had no material acquisitions or disposals of subsidiaries and affiliated companies.

Employee Information

As at 31 January 2004, the total remuneration to employees, including director's emoluments amounted to approximately HK\$6,401,000 (2003: approximately HK\$5,087,000). Remuneration is determined by reference to the performance, qualification and experience of individual employee and the prevailing industry practice. Other benefits include contributions to statutory mandatory provident fund scheme and medical coverage to its employees in Hong Kong and the statutory central pension schemes to its employees in the PRC. The Group had 1,046 employees (2003: 658) in Hong Kong and PRC.

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

During the period under review, Chengdu Mt. Green has sold 15.65 million of bottles of infusion medicine for the six months ended 31 January 2004. Compared with the sales of 24.84 million of bottles in corresponding period of last year, sales of human infusion medicine have been decreased by approximately 9.2 million of bottles or approximately 37%. This represented a drop of 45.6% in terms of turnover as compared with the corresponding period in the preceding year. There are three major reasons for the decrease. Firstly, the company intended to reduce operating risk by establishing stringent credit control on customers. As a result of setting up all these credit control measures, the turnover of the company decreased accordingly. Secondly, due to fierce market competition, in order to gain market shares, most of the competing manufacturers have reduced the sale prices of their products. The absolute amount of sales was then reduced. Moreover, the prices of raw materials increased during the period under review. These increases made the gross profit margin decrease by approximately 10.75% as compared with the corresponding period in the preceding year. Lastly, in considering of decreasing profit margin of infusion medicines, Chengdu Mt. Green reduced its production during the period under review and shifted its efforts towards products with higher profit margin.

Sichuan Future Industrial Co., Ltd. ("Sichuan Future")

For six-months period ended 31 January 2004, the sale of Sichuan Future decreased from approximately HK\$19,092,000 last year to approximately HK\$9,770,000 for the corresponding period this year, representing a decrease of approximately 48.8%. The decrease was mainly due to adverse market conditions and keen competition in the packaging material market. Profit margins of low end products are very slim, or even in a gross loss position.

To overcome the difficult market conditions, Sichuan Future reduced its production of low end products gradually and transformed its production to high end products in order to recover its loss and increase market penetration. As the product transformation is still in its early stage, it is inevitable that the sales volume of the company for the period under review was still quite low.

The aluminium plastic caps instead of natural rubber or purely aluminium cap used for anti-biotic powder injection and infusion medicine be compulsorily regulated by The State Food & Drug Administration (“SFDA”) by the end of the year 2004. In view of this new measure be enforced in the industry, the company does adopt a multilateral marketing strategy, Sichuan Future will continue to maintain the market share of traditional medical cap on one hand, and also devote its efforts to boost the sale of multi-coloured transparent aluminium-plastic caps on the other hand, so as to expand the market coverage of the company and achieve economies of scale. In addition, Sichuan Future during the period under review established its website, thereby enlarging the level of connection with and bases of customers and maintaining a close relationship with customers.

During the period under review, Sichuan Future successfully developed new innovative “tear and pull” aluminium-plastic cap. The new developed medical cap is mainly used for orally administrated liquid bottle. Compared with the traditional medical cap, the end-user could suck on the tube to draw up the orally administrated liquid drug without opening the outer-closure by ancillary accessories. The directors believe that the new product will provide Sichuan Future with the opportunities to co-operate with potential pharmaceutical companies in other major marketing regions, so as to reduce its reliance currently placed on the infusion medicine market.

Sichuan Future, during the period under review, continued to enhance the quality control procedure and achieve cost savings. Establishment of close relationship with the suppliers and on-going operation streamlining were the procedures adopted during the period under review.

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

Chengdu Yuan Heng recorded a turnover of approximately HK\$10,092,000 for the six months ended 31 January 2004, representing a decrease of 27.3% as compared with that for the corresponding period in the previous year. The decrease was mainly due to the change of governmental policy on packaging of veterinary drug by the Ministry of Agriculture, which cause products with old packaging be therefore returned to the factories for re-packaging. As a result, Yuen Heng has suffered losses on the repackaging of products and slowed down the market promotion for products, which was a factor causing

the decline in turnover on one hand. On the other hand, as most of the veterinary drug manufacturers have to pass the GMP certification before 2005, those small non-GMP compliant manufacturers reduced the selling prices of their veterinary drugs significantly in order to sell all the remaining stock before the due date. Chengdu Yuan Heng during the period under review has therefore reduced the selling prices of its products and suffered losses in sales and profit accordingly.

Research and development of new veterinary drugs will still be the key task for Yuen Heng in the year 2004, while the development of veterinary drugs used for cow and beef will be one of key research projects in the year 2004, thereby enlarging the product portfolio of the company. Moreover, the company will continue to hold certain technical conferences for the purpose of promoting the company's drugs in the year 2004 so as to widen its sale channel, and also enhance the company's image.

The legal procedures for the acquisition of 四川利亨生物藥業有限公司 (formerly named as Sichuan Animal Medicine Factory) were all completed in December 2003, the production permit and the approval for transferring 18 vaccines to 四川利亨 was also obtained from the relevant authority in December 2003. The production lines become operative in January 2004.

Sichuan Shule Pharmaceutical Joint Stock Company Limited (“Sichuan Shule”)

Compared with the two month's turnover of approximately HK\$13,130,000 included in the consolidated turnover of the Group for the year ended 31 July 2003, the sale of Sichuan Shule was increased to approximately HK\$58,780,000. The improvement in the company's result was largely attributable to the efforts made by the management and the staff that have helped to expedite the pace of business development of the company. Moreover, the company made timely adjustments to marketing strategies and product mix in accordance with the changing trend of pharmaceutical market.

In order to further enhance the competitiveness of its product in increasingly competitive market, Sichuan Shule endeavoured to accelerate its step towards the development of new products. The company also strengthen the quality control procedures and continuously optimise and rationalize its production processes, while production technology are updated accordingly, and logistic processes and production planning are reviewed periodically, with a view to achieving overall cost savings and providing a solid platform for future growth of the company.

The modification for the polypropylene bottle production line was completed and production permit was obtained from SFDA in September 2003. The company believe that the addition of this production line will provide it with another main source of income.

The GMP modification project for solid medicine workshop is still in progress. The project is expected to be completed by the end of April 2004 and GMP certification will be attained. As a result of GMP modification, the workshop's productivity will be further enhanced and the product mix of Sichuan Shule optimised.

Research and Development

Human drug:

Currently, the research and development projects undertaken by Sichuan Shule are progressing well. About 9 drugs in 11 dimensions therein were submitted to SFDA for application for certification registration. The application for clinical test for Fructose Injection and Propofol during the period under review had been approved by the relevant authority. The result in respect of pre-clinical tests for Glucose and Sodium Chloride Potassium Chloride Injection, Ribavirin and Glucose Injection, Matrine Sodium Chloride Injection, Zedoary Turmeric Oil and Glucose Injection (10ml), and Propofol Injection (10ml) were also reported to SFDA for drug supervision.

Apart from keeping on the research and development of the existing on-going projects, Chengdu Mt. Green also during the period under review proceeded to introduce and develop natural pharmaceutical products. Until the date of this announcement, certain applications for new medicine certificates are still pending the approval from SFDA.

Veterinary drug:

During the period under review, 13 products had obtained pharmaceutical registration, namely Ribavirine Injection, Enrofloxacin for injection, Doxycycline Hyclate for injection, Compound Gentamycini-micronomicini Sulfatis Injection, An Qing Fen Zhen, Estradiol Benzoate Injection, Compound Ciprofloxacin Hydrochloride-II Injection, Shuanghuanglian Zhushuye, Compound Herba Senecionis Scandentis Injection, Compound Ciprofloxacin Hydrochloride Injection, Spectinomycin Hydrochloride and Lincomycin Hydrochloride Injection, Compound Thiamphenical Injection, and Compound Kanamycin Sulfate Suspension Injection.

Of those new registrations, Shuanghuanglian Zhushuye and Compound Herba Senecionis Scandentis Injection are innovative products of pure traditional Chinese medicine compound. The products were developed in co-operation with Sichuan Medical College for Animal Husbandry.

OUTLOOK

Sichuan Shule, as one of the leading manufacturers of nutritional infusion medicines (e.g. amino acids and fat emulsion solutions) and non-addictive anesthetics in the PRC, the company will continuously strive to broaden its revenue base by introducing more new products. Concurrently, Sichuan Shule will continue to leverage on its advanced technology and research prowess to enhance competitiveness. In view of increasingly changing market, suitable adjustments in product mix and development of advanced and high value-added products will be undertaken, so as to effectively react to the market change and maintain a sustained growth in the sales of the company.

To improve profitability, Chengdu Mt. Green has commenced taking further initiatives to (i) maintain market share in existing infusion medicine market and gradually expand to other potential market in order to explore and broaden the market coverage; (ii) improve production efficiency and enhance quality management; and (iii) adjust the existing product mix and gradually transform into natural pharmaceutical products. In order to accelerate the pace of product transformation, the company plans to secure strategic alliances from the international arena so that the company will be able to develop and introduce more value added natural pharmaceutical products, thereby broadening the product portfolio and improve the earning base of Chengdu Mt. Green.

As the development of modernized agriculture and husbandry industry becomes one of prime directives of the PRC government, it is evident that demand for modern vaccine products of international standards is growing in intensity as the industry develops. Chengdu Yuan Heng holds one of the 28 vaccine production licenses in the PRC, the directors believe with this inherent advantages, the accelerated related construction of new GMP-compliant vaccine factories would further consolidate its foundation in sustained growth in the future. Also by the end of 2005, non-GMP compliant veterinary drug manufacturers will be gradually closed down, and only manufacturers able to uphold stringent production standards, such as Chengdu Yuan Heng, will be in good positions to benefit from the more mature and regulated market.

As to Sichuan Future, the company will continue to accelerate the pace of new product development on one hand. On the other hand, Sichuan Future will closely observe the changes in the market, review the marketing strategy from time to time so as to enhance its competitiveness and profitability of the company. Moreover, continued implementation of stringent cost control measures and improvements in management systems efficiency will be pursued. Following the imposition of new state policy on medical caps for anti-biotic powder injection applications and infusion medicine applications thereafter in April 2004, the directors are confident that the competitive edge of Sichuan Future can be further enhanced.

USE OF PROCEEDS FROM THE PLACING OF NEW SHARES

From the date of listing on April 2001, the Group invested approximately HK\$4.3 million, HK\$20.4 million, HK\$18 million and HK\$1.5 million on various projects in the financial years ended 2001, 2002, 2003, and for the period ended 31 January 2004 respectively. The use of proceeds for the period ended 31 January 2004 was mainly used for purchase of production equipment.

COMPETING INTEREST

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

DIRECTORS' AND CHIEF EXECUTIVES' INTEREST IN THE SHARES OF THE COMPANY

As at 31 January 2004, the interests or short positions of the directors and chief executives of the Company in the shares, underlying shares and debentures of the Company or any of its associated corporations (within the meaning of Part XV of the Securities and Futures Ordinance ("SFO")) which were notified to the Company and the Stock Exchange pursuant to Division 7 and 8 of Part XV of the SFO (including interests or short positions which they were taken or deemed to have under such provisions of the SFO), or which were required to be entered into the register required to be kept by the Company, pursuant to Section 352 of the SFO, or which were required, pursuant to Rules 5.40 to 5.58 of the GEM Listing Rules, to be notified to the Company and the Stock Exchange, were as follows:

| Name of Director | Capacity and nature of interest | Number of shares in the Company | Percentage of the Company's issued capital |
|------------------------------------|---------------------------------|---------------------------------|--|
| Mr. Wong Sai Chung (<i>Note</i>) | Through controlled corporations | <u>400,000,000</u> | <u>80</u> |

Note: The interests in the shares of the Company attributable to Mr. Wong Sai Chung, an executive director, are held through Concord Pharmaceutical Technology (Holdings) Limited and Concord Business Management Limited. Concord Pharmaceutical Technology (Holdings) Limited and Concord Business Management Limited are investment holding companies wholly-owned by Mr. Wong Sai Chung.

Pursuant to the terms of the Company's Pre-IPO Share Option Scheme (the "Pre-IPO Plan") adopted by the Company on 23 March 2001, the Company has granted options to the following directors to subscribe for shares in the Company at any time from 10 October 2001 up to and including 22 March 2011 at an exercise price of HK\$0.55 per share. Summarized details of the options which remain outstanding as at 31 January 2004 are as follows:

| Name of Director | Number of underlying shares |
|-------------------------|------------------------------------|
| Mr. Wong Sai Wa | 3,200,000 |
| Mr. Kwan Kai Cheong | <u>3,000,000</u> |

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

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

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

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

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

The interests of the directors in share options granted by the Company are separately disclosed in the section "Share option schemes" in this report.

Save as disclosed above, as at 31 January 2004, none of the directors or chief executive of the Company had any interest or short position in the shares, underlying shares or debentures of the Company or any of its associated corporations (within the meaning of Part XV of the SFO) which would have to be notified to the Company and the Stock Exchange pursuant to Divisions 7 and 8 of Part XV of the SFO (including interests or short positions which they were taken or deemed to have under such provision of the SFO) or which were required to be kept under Section 352 of the SFO or as otherwise notified to the Company and the Stock Exchange pursuant to the minimum standards of dealing by directors of listed issuers as referred to in Rules 5.40 to 5.58 of the GEM Listing Rules.

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

SHARE OPTION SCHEMES

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

Pursuant to the Pre-IPO Plan, five employees of the Group (including two executive Directors) were conditionally granted options on 23 March 2001 to subscribe for an aggregate of 7,400,000 shares, which upon exercise in full will result in issue of 7,400,000 additional ordinary shares of HK\$0.05 each for aggregate proceeds of HK\$4,070,000 before the related shares issue expense. All of these options have a duration of 10 years from the date of grant of the options, and each option is exercisable in accordance with the terms of issue after 6 months from the date of listing of the shares on GEM, but each shall lapse if the relevant grantee ceases to be employed by the relevant companies. The options of 400,000 shares granted to Ms Yip Yuk Lin and Dr. Chan Ka Keung respectively were cancelled due to their resignation from the Group. Accordingly, as at 31 January 2004, the number of share options granted to the employees remained 6,600,000 shares. An aggregate amount of HK\$3,630,000 will be generated if all share options are fully exercised. As at 31 January 2004, none of the directors or employees of the Company had exercised any share options and no allotment or issue of shares was made pursuant to the Pre-IPO Plan.

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

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

INTEREST DISCLOSEABLE UNDER THE SFO AND SUBSTANTIAL SHAREHOLDERS

So far as is known to any director or chief executive of the Company, as at 31 January 2004, shareholders (other than directors or chief executive of the Company) who had interests or short positions in the shares or underlying shares of the Company which would fall to be disclosed to the Company under the provisions of Divisions 2 and 3 of Part XV of the SFO or, directly, or indirectly, interested in 10% or more of the nominal value of any class of share capital carrying rights to vote on all circumstances at general meeting of any other members of the Group were as follows:

| Name of shareholder | Company/ Name of Group member | Capacity | Number of shares held | % of shareholding |
|--|--|---|----------------------------------|------------------------------|
| Concord Pharmaceutical Technology (Holdings) Limited (<i>Note</i>) | Company | Beneficial owner | 400,000,000 | 80 |
| Concord Business Management Limited (<i>Note</i>) | Company | Interest of a controlled corporation | 400,000,000 | 80 |
| Mr. Wong Sai Chung (<i>Note</i>) | Company | Interest of a controlled corporation | <u>400,000,000</u> | <u>80</u> |

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

As at 31 January 2004, Mr. Wong Sai Chung, Concord Business Management Limited and Concord Pharmaceutical Technology (Holdings) Limited were, or were taken to be, interested in the Convertible Note referred to in the section "Directors' and Chief Executives' interests in the Shares of the Company" in this report.

Save as disclosed above, as at 31 January 2004, the directors or chief executives of the Company were not aware of any other person (other than directors or chief executives of the Company) who had an interest or short position in the shares or underlying shares of the Company which would fall to be disclosed to the Company under the provisions of Divisions 2 and 3 of Part XV of the SFO, or who was interested in 10% or more of the nominal value of any class of share capital carrying rights to vote in all circumstances at general meeting of any other member of the Group.

AUDIT COMMITTEE

The Company set up an audit committee on 23 March 2001 with written terms of reference in compliance with the requirements as set out in Rules 5.23, 5.24 and 5.25 of the GEM Listing Rules. The audit committee has 2 members, namely Mr. Tsim Tak-Lung Dominic and Mr. Chow Wai Ming, both being independent non-executive directors. The primary duties of the audit committee are to review and supervise the financial reporting process and internal control of the Group, and to review the Group's annual reports and accounts, and half yearly and quarterly reports.

COMPLIANCE WITH BOARD PRACTICE AND PROCEDURES

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 for the period under review.

PURCHASE, SALE OR REDEMPTION OF THE COMPANY'S SHARES

During the six months ended 31 January 2004, neither the Company nor any of its subsidiaries had purchased, sold or redeemed any of the Company's listed securities.

By Order of the Board
Wong Sai Chung
Chairman

Hong Kong, 15 March, 2004