Medical China Limited

(incorporated in Bermuda with limited liability)

Annual report 2003

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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

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

Canon's Court
22 Victoria Street
Hamilton HM12
Bermuda

HONG KONG SHARE REGISTRAR

Computershare Hong Kong Investor Services 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

I hereby present to the shareholders the annual report of the Group for the year ended 31 December 2003.

RESULT ANALYSIS

For the year ended 31 December 2003, the Group recorded a turnover of HK$33,937,000, representing a decrease of 31.9% over the year of 2002. Loss attributable to shareholders were approximately HK$21,316,000, compared with a profit of approximately HK$22,979,000 recorded by the Group for the corresponding period in 2002.

BUSINESS REVIEW

As at 31 December 2003, the Group still maintained cooperation agreements with 65 hospitals respectively in the PRC. Under the impact of the Severe Acute Respiratory Syndrome ("SARS"), the Group's ray frequency ("RF") tumour therapeutic business was seriously dampened and recorded a drop for the first and second quarters. Business volume did not rebound until the third quarter, yet still decreased by 31.9% as compared with the corresponding period last year.

Meanwhile, the Group had achieved further progress in the research, development and production of Chinese drugs and chemical drugs and biochemical examination instruments through its subsidiaries, China Best Drugs Research (Nanjing) Limited ("China Best") and Sino-Innova Medical Science & Technology Co., Limited ("Sino-Innova"). This laid a good foundation for the Group's future expansion.

BUSINESS OUTLOOK

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

Medical equipment and drug businesses are fast growing. There are keen and tough competitors to attempt to share the market. Innovation and research efforts are the means to keep the Group competitive. Therefore, we are always to keep abreast of up-to-date information on advanced technology for medical equipment and anti-cancer drugs in order to improve our products and services.

On top of these, the Board of Directors (the "Board") will keep on diversifying the Group's business to broaden our client base and revenue sources. We will continue to develop the business of our subsidiaries of China Best and Sino-Innova which were formed on late 2002.

The Board perceived that these subsidiaries will enlarge the development of the medical equipment and drugs of the Group. All these will in turn transform into enhanced revenue source to 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 and advanced treatment technology, I am confident that the Group will have better success in the coming years.

ACKNOWLEDGEMENT

I hereby express my gratitude to all the directors for their contributions, and on behalf of the Board, 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

29 March 2003

MANAGEMENT DISCUSSION AND ANALYSIS

Financial Review

The Group's annual turnover for the year ended 31 December 2003 was HK$33,937,000, representing decrease of 31.9% over the corresponding year in 2002. For the year ended 31 December 2003, the Group's net loss attributable to shareholders amounted to HK$21,316,000 while profit attributable to shareholders of about HK$22,979,000 was recorded for the year ended 31 December 2002.

The decrease in turnover was mainly attributable to the fact that cancer patients avoided going to hospitals as much as possible after the outbreak of SARS during the first half of 2003. This resulted in a significant decrease in the number of treatments carried out at the RFAS centers set up by the Group and its contracted hospitals. Although the situation improved in the second half of the year, the turnover for the year was still comparatively lower than that of 2002. No new contracted hospital joint with the Group during the year also deteriorated the situation. Due to these factors, together with an impairment loss on intangible assets (which was made according to the Group's accounting policy and for prudent sake), the Group recorded a loss attributable to shareholders of HK$21,316,000 during the year.

In 2003, the Group acquired certain in-process medical research projects. The acquisition cost was allocated to each individual medical research project based on its estimated fair value at the acquisition date, after having taking into account an independent valuation of these medical research projects. At 31 December 2003, the directors of the Company reviewed the carrying value of these medical research projects individually, taking into account an updated independent valuation report, the future development resources required, the stage of completion and the risks surrounding the successful development and commercialization. Based on the review, the directors have recognized an impairment loss of $27,625,000 in respect of certain projects during the year ended 31 December 2003.

In relation to the remainder of the projects, whilst there is inherent uncertainty over the ultimate outcome of these projects, based on their assessment, the directors believe that there are currently no indications that they may be impaired.

The basic loss per share was 2.55 Hong Kong cents, while basic earnings per share in the corresponding year in 2002 was 2.82 Hong Kong cents.

CAPITAL STRUCTURE

As at 31 December 2003, the total number of issued ordinary shares and the issued share capital of the Company were 835,000,000 (2002: 835,000,000) and HK$8,350,000 (2002: HK$8,350,000) respectively.

FINANCIAL RESOURCES, BORROWINGS, BANKING FACILITIES AND LIQUIDITY

As at 31 December 2003, the Group had total assets of HK$179,614,000 (2002: HK$163,007,000) which were financed by current liabilities of HK$62,709,000 (2002: HK$28,455,000) and shareholders' equity of HK$112,843,000 (2002: HK$134,552,000).

The current assets of the Group amounted to approximately HK$101,516,000 (2002: HK$147,229,000) of which approximately HK$87,899,000 (2002: HK$107,218,000) were cash and bank deposits. The Group had no non-current liabilities or bank loans as at end of both years. The current liabilities of the Group amounted to approximately HK$62,709,000 (2002: HK$28,455,000) of which approximately HK$48,771,000 (2002: HK$15,786,000) were trade and other payables and HK$12,660,000 (2002: HK$10,212,000) was provision for income tax.

The Group generally finances its operations with internally generated resources. The Group's policy is to place surplus fund with banks as deposits with maturity within one year. None of Group's assets are charged to secure the Group's banking facilities. Furthermore, the Group had no long term borrowings. The gearing ratio calculated on the basis of banking facilities is nil (2002: nil).

The net asset per share as at 31 December 2003 was HK$0.14 (2002: HK$0.16).

CAPITAL COMMITMENT, SIGNIFICANT INVESTMENTS AND MATERIAL ACQUISITIONS AND DISPOSALS

On 17 January 2003, a wholly owned subsidiary named as Tat Lung Treatment (Shenzhen) Limited ("達隆醫學技術(深圳)有限公司") with registered capital of US$300,000 was incorporated and it was principally planned to focus on various kinds of medical software including RFAS software, biochemical analyzer control software and software of medical imaging analysis series.

On 7 April 2003, the Company's interest in Sino-Innova had reduced from the former 90% to 65%, while Nanjing-Innova Medical Science & Technology Co. Ltd., the PRC joint venture partner, increased its equity interest in Sino-Innova to 35%.

On 6 December 2002, the Company entered into a research projects acquisition and reorganisation agreement ("the Agreement") with Miss Guo Ping for the acquisition of 75% interest in 16 medicine research projects ("the Medicine projects") for a consideration of US$8,000,000. The transfer of ownership was completed by 10 June 2003.

Pursuant to the Agreement, the Company agreed to sell all the equity interest in China Best to Believe Investments Limited ("Believe Investments") after completion in exchange for Believe Investments issuing certain number of shares to the Company. Such shares represent 75% of the total issued capital of Believe Investments as enlarged by the issue. On completion of the reorganization, China Best became a wholly-owned subsidiary of Believe Investments and the Company holds 75% of the total enlarged issued share capital of Believe Investments. As a result, the Company indirectly has a 75% interest in the Medicine projects and the remaining

25% interest is retained indirectly by Ms. Guo Ping through the 25% shareholding in Believe Investments. Details of the Agreement were set out in the circular of "Discloseable Transaction" dated 8 January 2003.

The reorganisation pursuant to the Agreement was completed on 17 November 2003 and a new subsidiary named Medical China Technology Limited (formerly named as Believe Investments Limited) was acquired at the same date.

Apart from the aforesaid investments in subsidiaries, the Company had no other significant investment and there was no other material acquisitions and disposals of subsidiaries and affiliated companies in the course of the year.

As at 31 December 2003, the Group had outstanding capital commitment of approximately HK$11,700,000 (2002: HK$5,415,000).

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 2003, the Group did not have outstanding hedging instruments (2002: nil).

EMPLOYEES' INFORMATION AND BENEFIT SCHEME FOR THE EMPLOYEES

As at 31 December 2003, the Group has 134 (2002: 128) employees. The total of employee remuneration, including that of the Directors, for the year ended 31 December 2003 and 2002 amounted to HK$3,976,000 and HK$3,223,000 respectively.

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

Pursuant to the relevant labor rules and regulations in the PRC, the PRC subsidiary of the Group participates in a defined contribution retirement benefit scheme (the "Scheme") organized by the municipal government whereby the subsidiary is 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

As at 31 December 2003, the Group and the Company did not have any outstanding contingent liabilities (2002: nil).

BUSINESS REVIEW

During the year under review, the majority of the Group's sales and operating revenues were derived from provision of medical equipment and the relevant auxiliary services to the RF tumour therapeutic centers established by various hospitals in the PRC.

Meanwhile, the Group has achieved further progress in the research, development and production of Chinese drugs and chemical drugs and biochemical examination instruments through its subsidiaries China Best and Sino-Innova. This laid a solid foundation for the Group's long-term revenues in future.

Under the impact of SARS, the Group's RF tumour therapeutic business was seriously dampened and recorded a drop for the first and second quarters. Business volume didn't rebound until the third quarter, yet still decreased by 31.9% as compared with the corresponding period last year.

Below is a summary of the Group's developments during the year:

Development of the market and application of RFAS in the PRC

As at 31 December 2003, RFAS ray frequency tumour therapeutic centers established by Medical Treatment Technology (Shenzhen) Limited ("Tat Lung Shenzhen"), the Group's subsidiary, with hospitals in Mainland China remained at 65. Total revenues from RFAS treatment of therapeutic patients was HK$18,437,000, while total revenues from sales of electrode acuses and electric plates amounted to HK$7,181,000 and HK$137,000 respectively.

In view of the new distribution strategies of Boston Scientific Asia Pacific and the holding company of Radio Therapeutics in relation to RFAS products, details of which are stated in the circular captioned "Change in General Character or Nature of Business" dated 7 July 2003 ("Circular"), the Group has signed an agency agreement with Rex Medical in the USA for the exclusive sales in mainland China of its products, another surgery instrument for MicroPort treatment of lung and liver cancers. The agency agreement was for a term of three years.

Research, development and sales of drugs

The Group's subsidiary, China Best, has commenced the research and development of 16 new drugs as scheduled. One of the projects has obtained approval from the relevant authority in Jiangsu province, and will soon be reported to the State Food and Drug Administration for approval of clinical trial. Another two Chinese drugs have obtained approvals for clinical trial. The Company is planning to cooperate with certain pharmaceutical factories in the PRC in areas of clinical trial and production and sales. After due evaluation of the conditions of the current chemical drugs market, the Group has decided to temporarily postpone the research and development of seven of the drugs (including five chemical drugs) in order to concentrate the resources on the research and development of principal products. During the year, the Group has made full provision for impairment of the aforesaid seven drugs based on the Group's accounting policy and for prudent safe.

Research and development of 3-dimensional laparoscope and software for medical devices

Prototype of the 3-dimensional laparoscope developed by the Group was produced and has undergone further testing and improvement.

The Group has completed the software system for two medical testing instruments and obtained the relevant approval from government authority.

Research, development and production of medical testing instruments

Sino-Innova under the Group has commenced the production of various instruments, such as biomedical analyzers, immune analyzers, gene analyzers and blood analyzers. The new factory with an area of 8,000 square metres has been put into operation. The company has obtained the ISO9001 certification, and is applying for the CE certification in Europe and FDA certification in the USA. It was awarded the "Science and Technology Fund Prize" by Nanjing municipal government, while its general manager has obtained the "Award for Persons with Contribution to the Construction of New Nanjng City". During the year, Sino-Innova has participated in the international medical treatment exhibitions held respectively in Beijing, Chengdu and Nanjing in China, and in the USA, German, Korea, the UAE, Malaysia and Tanzania. The exhibited products were sold to various countries such as the USA, Italy, Poland, India, Pakistan, Thailand, German and Russia.

Others

Conducted by the research institute established by the Group with the Chengdu Military Hospital in China, the 28 animal trials using the self-developed new RFAS ray frequency tumour therapeutic instruments was successfully completed with satisfactory results.

Outlook and future strategies

With it existing business model confirmed, the Group will, on the base of its existing business, further ride on and expand its current business network to include more medical treatment instruments and service projects, so as to achieve the long-term stable revenue increase as summarized below:

The Group will further promote the ray frequency tumour therapeutic technology together with the intervention therapy technology to enhance the curing effects and increase revenues.

Active promotion will be carried out for the MicroPort tumour therapeutic instruments of the Rex Medical in the USA. Examination and approval procedures as well as preliminary promotion for the products will be completed as soon as possible. Action will be pursued for the sales of the products to hospital in the third quarter of next year.

The Group has obtained patents for its newly developed RFAS tumour therapeutic instruments and auxiliary devices, and will apply for approval of clinical trial in due course, so as to formally put the product to mass production in the second half of the year.

Production capacity of Sino-Innova will be further enhanced to increase the sales at home and abroad. Meanwhile, it planned to develop two to three new products and to control production cost in order to enhance profit margin.

China Best will continue to complete the research and development of a new drug and its application procedures for approval. Meanwhile, transference of established development technology will be stepped up to increase the Group's revenues.

Effort will be made to accelerate completion of the trial of 3-dimensional laparoscope and its examination and approval procedures, so that mass production can be carried out as soon as possible.

Business objectives in comparison with Actual Business Progress

Business plan	Business objectives for the nine-month period ended 31 December 2003 as stated in the circular captioned "Change in General Character or Nature of Business"	Actual business progress made in the nine-month period ended 31 December 2003
Continual development of the market and application of RFAS in the PRC	Entering into new contracts with six hospitals	No Increase of new hospital during the period. The total contracted hospital is 65 at the end of 2003.
	Establishing three RFAS training center	Established one RFAS training center in Lanzhou city.
	Hosting six conferences to demonstrate and promote the application of RFAS and providing training to doctors from nine contracted hospitals.	Hosted two conferences and provided training to doctors from three hospitals.
	Continuing the research and development of electrode and electric plates.	Research and development is in progress.

Business plan	Business objectives for the nine-month period ended 31 December 2003 as stated in the circular captioned "Change in General Character or Nature of Business"	Actual business progress made in the nine-month period ended 31 December 2003
Research, development and sales of drugs	Continuing the research and development of 16 medical research projects in relation to 16 different drugs after completion of acquisition of those projects; starting the testing of two drugs.	Research of 10 projects continues (of which 2 have obtained approval for clinical trial; application for clinical trial of one new drug has been made) and 7 projects temporarily postponed.
	Continuing cooperation with the Medical School of Fudan University (and other university(ies) in the PRC, if applicable) and identifying and continuing research and development topics	The agreement with the Medical School of Fudan University for research and development of new drugs is temporarily suspended after due evaluation.
	Developing sales network of ancillary anti-cancer medicine, and continuing the sales of ancillary anti-cancer medicine.	Sales networks of about 60 pharmaceutical stores for selling the medicine in the East China region have no improvement in store number and sales amount and some shop stop their selling and agents for the sales of ancillary anti-cancer medicine have been appointed.
	Negotiating with relevant parties regarding establishment of factory for production of drugs, applying to relevant authorities in relation to the establishment of factory for production of drugs, commencing and continuing construction of factory.	Repeated negotiations on construction of drug factory are underway and the project is under evaluation.

Business plan	Business objectives for the nine-month period ended 31 December 2003 as stated in the circular captioned "Change in General Character or Nature of Business"	Actual business progress made in the nine-month period ended 31 December 2003
Research and development of 3-dimensional laparoscope and software for medical devices	Completing prototype of 3-dimensional laparoscope; testing and revising prototype of 3-dimensional laparoscope.	Production of prototype of 3-dimensional laparoscope has completed, and the 3-dimensional laparoscope has been tested and improved.
	Developing, continuing development and completing development of software for medical devices.	Development of the software systems for two medical examination equipment is completed, and permits from governmental authority have been obtained.
Research, development and production of medical testing instruments	Producing Biochemistry Analyzer; obtaining the license for production of Coagulometer and producing Biochemistry Analyzer and Coagulometer; obtaining the license for production of Immunity Analyzer and producing Biochemistry Analyzer, Coagulometer and Immunity Analyzer.	Biochemistry Analyzer has been produced; license for production of Coagulometer has been obtained; Blood Coagulation Tester has been produced; the 酶標 Immunity Analyzer has passed examination, pending issuance of license for production, others were in progress.
	Continuing and completing construction of a new factory for production of medical testing instruments, and commencing production in the new factory of medical testing instruments.	The new factory is completed and put into operation for production of medical testing instruments.

Use of Proceeds from the Public Offering ("IPO") and the Top-up Placing

Business plan	Amount to be used for the nine-month period ended 31 December 2003 as stated in the circular captioned "Change in General Character or Nature of Business" *(in HK$ millions)*	Actual amount used during the nine-month period ended as at 31 December 2003 *(in HK$ millions)*
Continual expansion of the market and application of RFAS in the PRC	12	3
Research, development and sales of drugs	26	2.5
Research and development of 3-dimentional laparoscope and software for medical devices	7.5	1
Research, development and production of medical testing instruments	13	6.0
General working capital	10.17	–

During the nine-month period ended, the Group has applied HK$12,500,000 for projects as stated in the circular dated 7 July 2003. The unused proceeds from the IPO and the Top-up Placing of shares of approximately HK$56,170,000 have been deposited in the Group's account in a licensed Bank. The Group will apply the unused proceeds of HK$56,170,000 according to the business plans set out in the circular captioned "Change in General Character or Nature of Business" dated 7 July 2003.

DIRECTORS

Executive Directors

Dr. Li Nga Kuk, James, aged 58, 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 42, 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 57, is an Executive Director and the 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 50, is an Executive Director and the 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 49, 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 64, 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 (Zhenjian Jiaxing 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.

Non-executive Director

Dr. Chen Minshan, aged 39, 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 64, 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. Huang was appointed on 10 December 2001.

Mr. Fan Wan Tat, aged 59, 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 41, 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

Ms. Guo Ping, aged 44, is the general manager of China Best Drug, a subsidiary of the Company. Ms. Guo is an recognized research analyst of medicine in the PRC.

Consultants

Dr. Chen Min Shan, aged 39, 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 60, 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 67, 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.

The directors hereby present their 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 2003.

PRINCIPAL ACTIVITIES

The principal activity of the Company is investment holding and the Group is principally engaged in the provision of medical equipment, other services and the sales of medical accessories and testing equipment in the People's Republic of China ("the PRC"). The principal activities and other particulars of its subsidiaries are set out in note 16 to the financial statements.

The Group's turnover for the year is principally attributable to the provision of medical equipment and other services, net of business tax and the sales value of medical accessories and testing equipment 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 loss of the Group for the year ended 31 December 2003 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 23 to 63.

DIVIDENDS AND RESERVES

The directors do not recommend the payment of any dividend for the year ended 31 December 2003.

Details of the movements in reserves of the Group and the Company during the year are set out in note 30 to the financial statements.

MAJOR CUSTOMERS AND SUPPLIERS

	Percentage of the Group's total	
	Sales	**Purchases**
The largest customer	6%	
Five largest customers in aggregate	20%	
The largest supplier		20%
Five largest suppliers in aggregate		57%

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.

CHARITABLE DONATIONS

No donation was made by the Group during the year (2002: $1,055,000).

FIXED ASSETS

Details of movements in fixed assets of the Group during the year are set out in note 13 to the financial statements.

SHARE CAPITAL

Details of the movements in share capital of the Company during the year are set out in note 29 to the financial statements.

BANK LOANS AND OTHER BORROWINGS

The Company and the Group had no bank loans and other borrowing as at 31 December 2003.

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, Tai 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. Chan Shut Li, William, Chan Siu Sun and Li Tao To, Titus 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 14 to 15.

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 two years commencing on 1 December 2002.

Save as aforesaid, no service contract, which is not determinable by the Company within one year without payment of compensation (other than statutory compensation of any director proposed for re-election at the forthcoming annual general meeting.

DIRECTORS' AND CHIEF EXECUTIVE'S INTERESTS AND SHORT POSITIONS IN SHARE, UNDERLYING SHARES AND DEBENTURES

At 31 December, 2003, the interests or short positions of the Directors and chief executive 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 as recorded in the register 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 as referred to in rule 5.40 of GEM Listing Rules were as follows:

Interest in the Company:

Name	Number of ordinary shares of HK$0.01 each (the "Shares") in the share capital of the Company held	Nature of interests	Percentage of interest
Dr. Li Nga Kuk, James	32,800,000	Personal	3.93%
Mr. Li Wo Hing	32,800,000 212,320,000	Personal Corporate *(Note 1)*	3.93% 25.43%
	Aggregate: 245,120,000		**Aggregate: 29.36%**
Mr. Ng Kwai Sang	32,800,000 212,320,000	Personal Corporate *(Notes 1 & 2)*	3.93% 25.43%
	Aggregate: 245,120,000		**Aggregate: 29.36%**
Mr. Li Tai To, Titus	16,400,000	Personal	1.96%
Mr. Chan Siu Sun	32,800,000	Personal	3.93%

Notes :

1. 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.

2. 212,320,000 shares are owned by PMM, which is in turn owned as to 35.71% by Mr. Ng Kwai Sang. Details of the interest of PMM in these Shares are also set out in the paragraph headed "Interest Disclosable Under the SFO and Substantial Shareholders" below.

Save as disclosed above , as at 31 December 2003, none of the Directors or chief executive of the Company had any interests or short positions in the shares, underlying shares and debentures of the Company or its associated corporations (within the meaning of Part XV of the SFO) which were required, pursuant to section 352 of the SFO, to be entered in the register referred to therein or were required, pursuant to rule 5.40 of the GEM Listing Rules relating to minimum standards of dealing by Directors, to be notified to the Company and the Stock Exchange.

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 2003, there was no share options outstanding.

DIRECTORS' RIGHTS TO ACQUIRE SHARES OR DEBT SECURITIES

On 14 December 2001, the Company had conditional 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 2003, 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 SFO Ordinance.

Save as disclosed above, 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 respective associates, including 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.

INTERESTS DISCLOSABLE UNDER THE SFO AND SUBSTANTIAL SHAREHOLDERS

At 31 December 2003, so far as is known to the Directors or chief executive of the Company, the following persons (other than a Director or chief executive of the Company) had an interest or short position in the Shares or underlying shares of the Company as recorded in the register required to be kept under section 336 of the SFO:

Name of Substantial Shareholder	No of Shares held	Capacity	Percentage of interests
1. PMM *(note)*	212,320,000	Beneficial owner	25.43%
2. China Equity Associates L.P.	85,200,000	Beneficial owner	10.20%

Note: As at 31 December 2003, PMM owned 212,320,000 Shares, representing approximately 25.43% of the issued share capital of the Company. The issued share capital of PMM is owned as to 35.71% by Mr. Ng Kwai Sang, as to 28.57% by Mr. Li Wo Hing, as to 17.86% by Dr. Li Nga Kuk, James, as to 8.93%, by Mr. Li Tai To, Titus and as to 8.93% by Mr. Li Yue Erth. Mr. Ng Kwai Sang and Mr. Li Wo Hing's indirect interests in these 212,320,000 Shares through PMM are also disclosed in the paragraph headed "Directors' and Chief Executive's Interests and Short Positions in Shares, Underlying Shares and Debentures".

Save as disclosed above, as at 31 December 2003, so far as is known to any Director or chief executive of the Company, no other person (other than a Director or chief executive of the Company) had an interest or short position in the Shares or underlying shares of the Company as recorded in the register required to be kept under section 336 of the SFO.

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.

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

During the year, neither the Company nor any of its subsidiaries purchased, redeemed or sold any of the Company's listed securities.

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 2003 are set out in note 32 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 four meetings during the year.

The Audit Committee Members have reviewed the annual report for the year ended 31 December 2003.

INTEREST OF SPONSOR

As at 31 December 2003, the Sponsor of the Company, Celestical 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 of member of the Group.

Celestical Capital Limited had entered into a sponsorship agreement with the Company whereby, for a fee, Celestical Capital Limited acted 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. There was no change in auditors in any of the preceding 3 years.

By order of the Board
Li Nga Kuk, James
Chairman

Hong Kong, 29 March 2004

KPMG

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

We have audited the financial statements on pages 23 to 63 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 solely to you, as a body, in accordance with Section 90 of the Bermuda Companies Act 1981, and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report.

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 2003 and of the Group's loss 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, 3 March 2003

For the year ended 31 December 2003
(Expressed in Hong Kong dollars)

	Note	2003 $'000	2002 $'000
Turnover	3 & 12	**33,937**	49,850
Cost of services/sales		**(15,309)**	(14,592)
Gross profit		**18,628**	35,258
Other revenue	4	**4,441**	4,814
Other net income	4	**772**	327
Selling and distribution expenses		**(3,961)**	(4,481)
Administrative expenses		**(10,940)**	(7,853)
Impairment loss on intangible assets	15	**(27,625)**	–
Other operating expenses		**(51)**	(78)
(Loss)/profit from operations		**(18,736)**	27,987
Finance cost	5(a)	**(136)**	–
Share of loss of an associate		**(12)**	(15)
(Loss)/profit before taxation	5	**(18,884)**	27,972
Income tax	6(a)	**(2,445)**	(4,993)
(Loss)/profit after taxation		**(21,329)**	22,979
Loss shared by minority interests		**13**	–
(Loss)/profit attributable to shareholders	9	**(21,316)**	22,979
(Loss)/earnings per share (in Hong Kong cents)			
Basic	10	**(2.55)**	2.82

The notes on pages 30 to 63 form part of these financial statements.

Consolidated Balance Sheet

At 31 December 2003
(Expressed in Hong Kong dollars)

	Note	2003 $'000	2003 $'000	2002 $'000	2002 $'000
Non-current assets					
Fixed assets	13(a)				
– Property, plant and equipment			24,243		22,608
Construction in progress	14		825		1,547
Intangible assets	15		58,537		–
Interest in an associate	17		435		447
Negative goodwill	18		(5,942)		(8,824)
			78,098		15,778
Current assets					
Inventories	19	4,685		1,648	
Trade receivables	20	5,442		3,398	
Other receivables and prepayments	22	3,415		34,557	
Amount due from a related company	23	75		408	
Deposits with banks	24	79,760		93,488	
Cash and cash equivalents		8,139		13,730	
		101,516		147,229	
Current liabilities					
Trade and other payables	25	48,771		15,786	
Amounts due to related companies	26	1,278		897	
Amount due to a director	27	–		1,560	
Current taxation	28	12,660		10,212	
		62,709		28,455	
Net current assets			38,807		118,774
Total assets less current liabilities			116,905		134,552
Minority interests		(4,062)		–	
NET ASSETS			112,843		134,552

At 31 December 2003
(Expressed in Hong Kong dollars)

	Note	2003 $'000	2003 $'000	2002 $'000	2002 $'000
CAPITAL AND RESERVES					
Share capital	29		8,350		8,350
Reserves	30(a)		104,493		126,202
			112,843		134,552

Approved and authorized for issue by the board of directors on 29 March 2004.

Li Nga Kuk, James
Chairman

Li Wo Hing
Director

The notes on pages 30 to 63 form part of these financial statements.

Balance Sheet

At 31 December 2003
(Expressed in Hong Kong dollars)

	Note	2003 $'000	2003 $'000	2002 $'000	2002 $'000
Non-current assets					
Fixed assets	13(b)		570		729
Investments in subsidiaries	16		15,413		14,830
			15,983		15,559
Current assets					
Amounts due from subsidiaries	21	75,096		27,891	
Other receivables and prepayments	22	13		30,836	
Cash and cash equivalents		1,312		8,657	
		76,421		67,384	
Current liabilities					
Trade and other payables	25	2,980		2,044	
Amounts due to subsidiaries	21	16,275		507	
Amount due to a director	27	–		1,560	
		19,255		4,111	
Net current assets			57,166		63,273
NET ASSETS			73,149		78,832
CAPITAL AND RESERVES					
Share capital	29		8,350		8,350
Reserves	30(b)		64,799		70,482
			73,149		78,832

Approved and authorized for issue by the board of directors on 29 March 2004.

Li Nga Kuk, James
Chairman

Li Wo Hing
Director

The notes on pages 30 to 63 form part of these financial statements.

Consolidated Statement of Changes in Equity

For the year ended 31 December 2003
(Expressed in Hong Kong dollars)

	Note	2003 $'000	2002 $'000
Shareholders' equity at 1 January		**134,552**	92,343
Net losses not recognized in the income statement			
– Exchange differences on translation of the financial statements of entities outside Hong Kong	30(a)	**(393)**	(29)
Net (loss)/profit for the year		**(21,316)**	22,979
Issue of share capital		**–**	19,259
Shareholders' equity at 31 December		**112,843**	134,552

The notes on pages 30 to 63 form part of these financial statements.

Consolidated Cash Flow Statement

For the year ended 31 December 2003
(Expressed in Hong Kong dollars)

	2003		2002	
	$'000	$'000	$'000	$'000
Operating activities				
(Loss)/profit before taxation	(18,884)		27,972	
Adjustments for:				
Depreciation	5,214		4,722	
Impairment loss on intangible assets	27,625		–	
Amortization of negative goodwill	(2,882)		(2,882)	
Amortization of intangible assets	58		–	
Profit on disposal of fixed assets	(772)		(327)	
Interest income	(1,493)		(1,898)	
Finance cost	136		–	
Share of losses of an associate	12		15	
Foreign exchange gain	(354)		(6)	
Operating profit before changes in working capital	8,660		27,596	
Increase in inventories	(2,478)		(780)	
Increase in trade receivables	(2,044)		(1,293)	
Decrease in other receivables and prepayments	741		12,997	
Increase in trade and other payables	10,311		5,792	
Decrease/(increase) in amount due from a related company	333		(408)	
Increase in amounts due to related companies	381		–	
(Decrease)/increase in amount due to a director	(1,560)		888	
Net cash from operating activities		14,344		44,792

Consolidated Cash Flow Statement

For the year ended 31 December 2003
(Expressed in Hong Kong dollars)

	2003		2002	
	$'000	$'000	$'000	$'000
Investing activities				
Capital expenditure				
– Fixed assets	(1,143)		(5,341)	
– Construction in progress	(3,805)		(1,547)	
Decrease/(increase) in placement of time deposits with banks	13,728		(76,516)	
Expenditure on intangible assets	(32,103)		(30,218)	
Interest received	1,493		1,350	
Proceeds from sales of fixed assets	821		758	
Repayment from third party	–		34,462	
Payment for purchase of interest in an associate	–		(462)	
Net cash used in investing activities		(21,009)		(77,514)
Financing activities				
Net proceeds from issuance of new shares	–		19,259	
Interest paid	(136)		–	
Capital injection of minority interests	1,210		–	
Proceeds from new bank loan	9,398		–	
Repayment of bank loan	(9,398)		–	
Net cash generated from financing activities		1,074		19,259
Net decrease in cash and cash equivalents		(5,591)		(13,463)
Cash and cash equivalents at 1 January		13,730		27,193
Cash and cash equivalents at 31 December		8,139		13,730

The notes on pages 30 to 63 form part of these 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, sale of testing equipment and provision of medical research and development 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 Hong Kong Financial Reporting Standards (which includes 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 consolidated 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 associate.

(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.

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.

Minority interests at the balance sheet date, being the portion of the net assets of subsidiaries attributable to equity interests that are not owned by the Company, whether directly or indirectly through subsidiaries, are presented in the consolidated balance sheet separately from liabilities and the shareholders' equity. Minority interests in the results of the Group for the year are also separately presented in the income statement.

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

(f) Interest in associate

An associate is an entity in which the Group 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 associate for the year.

Unrealized profits and losses resulting from transactions between the Group and its associate 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.

2. SIGNIFICANT ACCOUNTING POLICIES (continued)

(g) Fixed assets and depreciation

(i) 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(j)).

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

Land use rights	Over the remaining term of the lease
Medical equipment	Shorter of 6 years and the remaining terms of the agreements with hospitals
Buildings	Shorter of 50 years and the remaining terms of the lease
Office, computer and other equipment	5 years
Motor vehicles	5 years

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

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. Capitalization 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) Intangible assets and amortization

(i) Expenditure on research activities, undertaken with the prospect of gaining new scientific or technical knowledge and understanding, is recognized as an expense in the period in which it is incurred. Expenditure on development activities is capitalized if the product or process is technically and commercially feasible and the Company has sufficient resources and the intention to complete development. 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.

(ii) Medical research projects and other intangible assets that are acquired by the Group are stated in the balance sheet at cost less accumulated amortization (see note 2(i)(iv)) and impairment losses (see note 2(j)).

(iii) Subsequent expenditure on an intangible asset after its purchase or its completion is recognized as an expense when it is incurred unless it is probable that this expenditure will enable the asset to generate future economic benefits in excess of its originally assessed standard of performance and this expenditure can be measured and attributed to the asset reliably. If these conditions are met, the subsequent expenditure is added to the cost of the intangible asset.

(iv) Amortization of intangible assets is charged to the income statement on a straight-line basis over the assets' estimated useful lives as follows:

Medical research projects	5 to 10 years
Other intangibles	5 to 10 years

2. SIGNIFICANT ACCOUNTING POLICIES (continued)

(j) 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;

– intangible assets; 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 such 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).

(ii) Reversals of impairment losses

An impairment loss is reversed if there has been a favourable 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.

2. SIGNIFICANT ACCOUNTING POLICIES (continued)

(k) 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.

(l) 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.

(m) Income tax

(i) Income tax for the year comprises current tax and movements in deferred tax assets and liabilities. Current tax and movements in deferred tax assets and liabilities are recognized in the income statement except to the extent that they relate to items recognized directly in equity, in which case they are recognized in equity.

(ii) Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at balance sheet date, and any adjustment to tax payable in respect of previous years.

2. SIGNIFICANT ACCOUNTING POLICIES (continued)

(m) Income tax (continued)

(iii) Deferred tax assets and liabilities arise from deductible and taxable temporary differences respectively, being the differences between the carrying amounts of assets and liabilities for financial reporting purposes and their tax bases. Deferred tax assets also arise from unused tax losses and unused tax credits.

Apart from certain limited exceptions, all deferred tax liabilities, and all deferred tax assets to the extent that it is probable that future taxable profits will be available against which the asset can be utilized, are recognized. Future taxable profits that may support the recognition of deferred tax assets arising from deductible temporary differences include those that will arise from the reversal of existing taxable temporary differences, provided those differences relate to the same taxation authority and the same taxable entity, and are expected to reverse either in the same period as the expected reversal of the deductible temporary difference or in periods into which a tax loss arising from the deferred tax asset can be carried back or forward. The same criteria are adopted when determining whether existing taxable temporary differences support the recognition of deferred tax assets arising from unused tax losses and credits, that is, those differences are taken into account if they relate to the same taxation authority and the same taxable entity, and are expected to reverse in a period, or periods, in which the tax loss or credit can be utilized.

The limited exceptions to recognition of deferred tax assets and liabilities are those temporary differences arising from negative goodwill treated as deferred income and temporary differences relating to investments in subsidiaries to the extent that, in the case of taxable differences, the Group controls the timing of the reversal and it is probable that the differences will not reverse in the foreseeable future, or in the case of deductible differences, unless it is probable that they will reverse in the future.

The amount of deferred tax recognized is measured based on the expected manner of realization or settlement of carrying amount of the assets and liabilities, using tax rates enacted or substantively enacted at the balance sheet date. Deferred tax assets and liabilities are not discounted.

The carrying amount of deferred tax assets is reviewed at each balance sheet date and is reduced to the extent it is no longer probable that sufficient taxable profit will be available, to allow the related tax benefit to be utilized. Any such reduction is reversed to the extent that it becomes probable that sufficient taxable profit will be available.

2. SIGNIFICANT ACCOUNTING POLICIES (continued)

(m) Income tax (continued)

(iv) Current tax balances and deferred tax balances, and movements therein, are presented separately from each other and are not offset. Current tax assets are offset against current tax liabilities, and deferred tax assets against deferred tax liabilities if, and only if, the Company or the Group has the legally enforceable right to set off current tax assets against current tax liabilities and the following additional conditions are met:

- in the case of current tax assets and liabilities, the Company or the Group intends either to settle on a net basis, or realize the asset and settle the liability simultaneously; or

- in the case of deferred tax assets and liabilities, if they relate to income taxes levied by the same taxation authority on either;

  - the same taxable entity; or

  - different taxable entities, which in each future period in which significant amounts of deferred tax liabilities or assets are expected to be settled or recovered, intent to realize the current tax assets and settle the current tax liabilities on a net basis or realize and settle simultaneously.

(n) 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.

2. SIGNIFICANT ACCOUNTING POLICIES (continued)

(o) 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.

(ii) *Sales of goods*

Revenue is recognized when medical accessories or equipment 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.

(p) 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.

(q) Employee benefits

(i) Salaries, annual bonuses, paid annual leave 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 31.

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 enterprises 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.

(u) Segment reporting

A segment is a distinguishable component of the Group that is engaged either in providing products or services (business segment), or in providing products or services within a particular economic environment (geographical segment), which is subject to risks and rewards that are different from those of other segments.

In accordance with the Group's internal financial reporting system, the Group has chosen business segment information as the primary reporting format and geographically segment informational as the secondary reporting format for the purposes of these financial statements.

2. SIGNIFICANT ACCOUNTING POLICIES (continued)

(u) Segment reporting (continued)

Segment revenue, expenses, results, assets and liabilities include items directly attributable to a segment as well as those that can be allocated on a reasonable basis to that segment. For example, segment assets may include inventories, trade receivables and property, plant and equipment. Segment revenue, expenses, assets, and liabilities are determined before intra-group balance and intra-group transactions are eliminated as part of the consolidation process, except to the extent that such intra-group balances and transactions are between group enterprises within a single segment. Inter-segment pricing is based on similar terms as those available to other external parties.

Segment capital expenditure is the total cost incurred during the period to acquire segment assets (both tangible an intangible) that are expected to be used for more than one period.

Unallocated items mainly comprise financial and corporate assets, corporate and financing expenses and minority interests.

3. TURNOVER

Turnover represents service fees arising from the provision of medical equipment services and related accessories, net of respective taxes; the sales value of testing equipment, net of value added tax, and service fees arising from the provision of research and development services, net of business 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:

	2003 $'000	2002 $'000
Medical service fees and sales of related accessories	25,754	49,850
Sales of testing equipment	6,831	–
Research and development services	1,352	–
	33,937	49,850

4. OTHER REVENUE AND NET INCOME

	2003 $'000	2002 $'000
Other revenue		
Interest income	1,493	1,898
Amortization of negative goodwill	2,882	2,882
Others	66	34
	4,441	4,814
Other net income		
Net gain on sale of fixed assets	772	327
	772	327

5. (LOSS)/PROFIT BEFORE TAXATION

(Loss)/profit before taxation is arrived at after charging/(crediting):

	2003 $'000	2002 $'000
(a) Finance cost:		
Interest expense on bank borrowings	136	–
(b) Staff costs:		
Staff costs (including directors' remuneration in note 7)		
– wages and salaries	3,851	3,090
– staff retirement benefits	125	133
	3,976	3,223
Average number of employees during the year	134	128
(c) Other items:		
Cost of inventories	10,603	10,082
Depreciation	5,214	4,722
Auditors' remuneration		
– audit services	870	662
– other services	200	200
Operating lease charges in respect of office premises	1,159	712
Donation	–	1,055
Amortization of negative goodwill	(2,882)	(2,882)
Amortization of intangible assets	58	–
Research and development costs	131	188

6. INCOME TAX IN THE CONSOLIDATED INCOME STATEMENT

(a) Taxation in the consolidated income statement represents:

	2003 $'000	2002 $'000
Current tax – PRC		
Tax for the year	2,445	4,993

(i) 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% (2002: 15%).

No provision for PRC income tax has been made in respect of the Company's other PRC subsidiaries, China Best, Sino-Innova and Tat Lung Treatment (Shenzhen) Limited ("Tat Lung Treatment"), as they did not have assessable profits for the year determined in accordance with relevant income tax rules and regulations in the PRC.

(b) Reconciliation between tax expenses and accounting (loss)/profit at applicable tax rates:

	2003 $'000	2002 $'000
(Loss)/profit before tax	(18,884)	27,972
Notional tax on (loss)/profit before tax, calculated at the rates applicable to profits in the countries concerned	(3,842)	4,093
Tax effect of non-deductible expenses	7,291	1,001
Tax effect of non-taxable revenue	(1,004)	(101)
Actual tax expense	2,445	4,993

(c) No provision has been made for deferred taxation as the Group does not have any material deductible or taxable temporary differences.

7. DIRECTORS' REMUNERATION

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

	2003 $'000	2002 $'000
Executive directors		
Fees	–	–
Salaries and other emoluments	990	990
Retirement benefit scheme contributions	33	26
Bonus	83	83
	1,106	1,099
Non-executive directors		
Fees	240	240

The remuneration of the directors is within the following bands:

	2003 Number of directors	2002 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 2003.

8. INDIVIDUALS WITH HIGHEST EMOLUMENTS

Of the five individuals with the highest emoluments, four (2002: four) are directors whose emoluments are disclosed in note 7. The aggregate of the emoluments in respect of the remaining one (2002: one) individual is as follows:

	2003 $'000	2002 $'000
Basic salaries, allowances and other benefits	180	165
Discretionary bonuses	–	14
Retirement benefit scheme contributions	9	–
	189	179

The emoluments of the remaining one (2002: one) individual with the highest emoluments are within the following band:

	2003 Number of individuals	2002 Number of individuals
Nil – $1,000,000	1	1

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. (LOSS)/PROFIT ATTRIBUTABLE TO SHAREHOLDERS

The consolidated (loss)/profit attributable to shareholders includes a loss of $5,683,000 (2002: profit of $4,785,000) which has been dealt with in the financial statements of the Company.

10. LOSS/EARNINGS PER SHARE

(a) Basic loss/earnings per share

The calculation of basic loss per share for the year ended 31 December 2003 is based on the loss attributable to shareholders of $21,316,000 (2002: profit of $22,979,000) divided by the weighted average number of 835,000,000 (2002: 814,095,890) ordinary shares in issue during the year.

(b) Diluted loss/earnings per share

No diluted loss/earnings per share is shown as the Company had no dilutive potential ordinary shares as at 31 December 2003 and 2002.

11. CHANGES IN ACCOUNTING POLICY

In prior years, deferred tax liabilities were 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 were expected with reasonable probability to crystallize in the foreseeable future. Deferred tax assets were not recognized unless their realization was assured beyond reasonable doubt. With effect from 1 January 2003, in order to comply with Statement of Standard Accounting Practice 12 (revised) issued by the Hong Kong Society of Accountants, the Group adopted a new policy for deferred tax as set out in note 2(m)(iii). The adoption of this policy has no impact on the Group's results and net assets for the current and prior years. Accordingly, no prior period adjustments were made.

12. SEGMENT REPORTING

Segment information is presented in respect of the Group's business segments. Business segment information is chosen as the primary reporting format because this is more relevant to the Group's internal financial reporting. No segment information by geographical segments is presented as the Group operates in one single market, the PRC.

Business segments

The Group comprises the following main business segments:

Medical services: provision of medical equipment for the treatment of cancer.

Sales of medical equipment: manufacture and sale of medical equipment.

Research and development: development of drugs.

12. SEGMENT REPORTING (continued)

Business segments (continued)

	Medical services		Sales of medical equipment		Research and development		Consolidated	
	2003 $'000	2002 $'000	2003 $'000	2002 $'000	2003 $'000	2002 $'000	2003 $'000	2002 $'000
Revenue from external customers	25,754	49,850	6,831	–	1,352	–	33,937	49,850
Segment result	15,437	31,690	(1,085)	–	(28,682)	–	(14,330)	31,690
Unallocated operating income and expenses							(4,406)	(3,703)
(Loss)/profit from operations							(18,736)	27,987
Finance costs							(136)	–
Share of loss of an associate							(12)	(15)
Income tax							(2,445)	(4,993)
Loss shared by minority interests							13	–
(Loss)/profit attributable to shareholders							(21,316)	22,979
Depreciation for the year	4,709	4,722	224	–	281	–	5,214	4,722
Impairment loss for the year	–	–	–	–	(27,625)	–	(27,625)	–
Amortization for the year								
– negative goodwill	(2,882)	(2,882)	–	–	–	–	(2,882)	(2,882)
– intangible assets	58	–	–	–	–	–	58	–
Segment assets	15,738	17,196	15,543	–	59,857	30,218	91,138	47,414
Unallocated assets							88,476	115,593
Total assets							179,614	163,007
Segment liabilities	(18,109)	(11,495)	(4,482)	–	(21,284)	–	(43,875)	(11,495)
Unallocated liabilities							(18,834)	(16,960)
Total liabilities							(62,709)	(28,455)
Capital expenditure incurred during the year	–	6,212	7,904	–	84,987	676		

13. FIXED ASSETS

(a) The Group

	Land and buildings $'000	Medical equipment $'000	Office, computer and other equipment $'000	Motor vehicles $'000	Total $'000
Cost:					
At 1 January 2003	–	30,825	1,105	999	32,929
Additions	1,765	–	361	725	2,851
Transfer in from construction in progress *(Note 14)*	4,527	–	–	–	4,527
Disposals	–	(704)	–	–	(704)
Exchange adjustment	–	(64)	(4)	(1)	(69)
At 31 December 2003	**6,292**	**30,057**	**1,462**	**1,723**	**39,534**
Aggregate depreciation:					
At 1 January 2003	–	(10,058)	(126)	(137)	(10,321)
Charge for the year	(49)	(4,717)	(179)	(269)	(5,214)
Written back on disposal	–	231	–	–	231
Exchange adjustment	–	13	–	–	13
At 31 December 2003	**(49)**	**(14,531)**	**(305)**	**(406)**	**(15,291)**
Net book value:					
At 31 December 2003	**6,243**	**15,526**	**1,157**	**1,317**	**24,243**
At 31 December 2002	–	20,767	979	862	22,608

13. FIXED ASSETS (continued)

(b) The Company

	Office, computer and other equipment $'000	Motor vehicles $'000	Total $'000
Cost:			
At 1 January 2003	70	803	873
Additions	20	–	20
At 31 December 2003	**90**	**803**	**893**
Aggregate depreciation:			
At 1 January 2003	(10)	(134)	(144)
Charge for the year	(18)	(161)	(179)
At 31 December 2003	**(28)**	**(295)**	**(323)**
Net book value:			
At 31 December 2003	**62**	**508**	**570**
At 31 December 2002	60	669	729

(c) The land and buildings held by the Group at 31 December 2003 are under medium term lease outside Hong Kong.

(Expressed in Hong Kong dollars)

14. CONSTRUCTION IN PROGRESS

	The Group	
	2003 $'000	2002 $'000
Balance at 1 January	1,547	–
Additions	3,812	1,547
Transfer to fixed assets *(Note 13(a))*	(4,527)	–
Exchange adjustment	(7)	–
Balance at 31 December	825	1,547

15. INTANGIBLE ASSETS

	Medical research projects $'000	Others $'000	Total $'000
Cost:			
At 1 January 2003	–	–	–
Additions	83,901	2,327	86,228
Exchange adjustment	(8)	–	(8)
At 31 December 2003	**83,893**	**2,327**	**86,220**
Accumulated amortisation:			
At 1 January 2003	–	–	–
Charge for the year	–	(58)	(58)
Impairment loss	(27,625)	–	(27,625)
At 31 December 2003	**(27,625)**	**(58)**	**(27,683)**
Net book value:			
At 31 December 2003	**56,268**	**2,269**	**58,537**
At 31 December 2002	–	–	–

Impairment loss

In 2003, the Group acquired certain in-process medical research projects. The acquisition cost was allocated to each individual medical research project based on its estimated fair value at the acquisition date, after having taking into account an independent valuation of these medical research projects.

At 31 December 2003, the directors of the Company reviewed the carrying value of these medical research projects individually, taking into account an updated independent valuation report, the future development resources required, the stage of completion and the risks surrounding the successful development and commercialization. Based on the review, the directors have recognized an impairment loss of $27,625,000 in respect of certain projects during the year ended 31 December 2003.

In relation to the remainder of the projects, whilst these is inherent uncertainty over the ultimate outcome of these projects, based on their assessment, the directors believe that there are currently no indications that they may be impaired.

(Expressed in Hong Kong dollars)

16. INVESTMENTS IN SUBSIDIARIES

	The Company	
	2003 $'000	2002 $'000
Unlisted shares, at cost	**15,413**	14,830

Details of the subsidiaries at 31 December 2003 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.

		Percentage of equity						
Name of company	Place of incorporation/ establishment and operation	Group's effective holding	held by the Company	held by subsidiary	Issued capital	Registered capital	Principal activities	Note
Future Asia Management Ltd.	British Virgin Islands ("B.V.I.")	100%	100%	–	US$20,000	US$50,000	Investment holding	
Tat Lung Medical Treatment Technology Ltd.	Hong Kong	100%	–	100%	$142,900	$142,900	Investment holding	
Tat Lung Medical Treatment Technology (Shenzhen) Ltd.	PRC	100%	–	100%	$5,000,000	$5,000,000	Provision of medical equipment and related services	(i)
China Best Drugs Research (Nanjing) Ltd.	PRC	75%	–	100%	US$1,500,000	US$3,000,000	Research and development of medicine and drugs	(ii)
Sino-Innova Medical Science & Technology Co., Ltd.	PRC	65%	65%	–	US$1,500,000	US$1,500,000	Manufacturing and sale of medical equipment	(iii)
Medical China Technology Ltd. (formerly known as Believe Investments Ltd.)	B.V.I.	75%	75%	–	US$100	US$50,000	Investment holding	
Tat Lung Medical Treatment (Shenzhen) Ltd.	PRC	100%	100%	–	US$300,000	US$300,000	Development of software for medical equipment	(iv)

16. 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 center for medicine and drugs. During the year, the Company contributed US$999,982 as the capital contribution. Jiangsu Tianhuadapeng Certified Public Accountants Co. Ltd have verified the above capital contribution, and issued a capital verification report on 18 March 2003.

Pursuant to a research projects acquisition and reorganization agreement with Miss Guo Ping dated 6 December 2002, the subsidiary acquired certain medicial research projects from Miss Guo. Upon the completion of reorganization, the Company retains 75% shareholding in the subsidiary while the remaining 25% shareholding is held by Miss Guo.

(iii) The subsidiary is a sino-foreign enterprise set up to establish a medical equipment production line in Nanjing, the PRC. During the year, the Company contributed US$150,000 and US$125,000 respectively as the capital contribution. JiangSu XingGuang Certified Public Accountants and Nan Jing Zhong Cheng Yin Combined Certified Public Accountants have verified the above capital contributions, and issued capital verification reports on 31 March 2003 and 9 September 2003 respectively.

As at 31 December 2003, the Company's total investment in this subsidiary amounted to US$975,000.

(iv) The subsidiary is a wholly foreign owned enterprise established in Shenzhen Special Economic Zone in the PRC and set up to provide medical equipment software. During the year, the Company contributed US$300,000 as the capital contribution. Shenzhen Worldson Certified Public Accountants have verified the above capital contribution, and issued a capital verification report on 10 June 2003.

As at 31 December 2003, the Company's total investment in this subsidiary amount to US$300,000.

17. INTEREST IN AN ASSOCIATE

	The Group	
	2003	2002
	$'000	$'000
Share of net assets	**435**	447

17. INTEREST IN AN ASSOCIATE (continued)

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

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

The associate is a sino-foreign enterprise and set up to establish a drug and medicine production line in Jiangxi, the PRC. During the year ended December 2002, the Company contributed a total capital of RMB490,000 which has been verified by Yi Chun Zheng Xin Certified Public Accountants. The related capital verification report was issued on 20 August 2002. No further capital contribution has been made by the Company.

18. NEGATIVE GOODWILL

	Negative goodwill $'000
Cost:	
At 1 January 2003 and 31 December 2003	**(16,029)**
Accumulated amortization:	
At 1 January 2003	7,205
Amortization for the year	2,882
At 31 December 2003	**10,087**
Carrying amount:	
At 31 December 2003	**(5,942)**
At 31 December 2002	(8,824)

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"). It is recognized as income on a straight-line basis over five years.

19. INVENTORIES

	The Group	
	2003 **$'000**	2002 $'000
Raw materials	**1,143**	448
Work in progress	**1,094**	–
Finished goods	**2,448**	1,200
	4,685	1,648

All inventories are stated at cost.

20. TRADE RECEIVABLES

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

An ageing analysis of trade receivables is as follows:

	The Group	
	2003 **$'000**	2002 $'000
Within 3 months of the date of billing	**5,208**	3,398
3 to 6 months of the date of billing	**83**	–
6 to 12 months of the date of billing	**151**	–
	5,442	3,398

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

21. AMOUNTS DUE FROM/(TO) SUBSIDIARIES

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

22. OTHER RECEIVABLES AND PREPAYMENTS

	The Group		The Company	
	2003 **$'000**	2002 $'000	**2003** **$'000**	2002 $'000
Other receivables, deposits and prepayments	**3,415**	4,339	**13**	618
Acquisition deposit	**–**	30,218	**–**	30,218
	3,415	34,557	**13**	30,836

23. AMOUNT DUE FROM A RELATED COMPANY

	The Group	
	2003 **$'000**	2002 $'000
Innova Medical Science & Technology Company Limited ("Innova")	**–**	408
Wuzhou Tat Lung	**75**	–
Maximum amount outstanding during the year	**75**	408

Innova is the minority shareholder of a subsidiary, Sino-Innova.

The wife of Dr. Li Tai To, Titus was a major shareholder of Wuzhou Tat Lung and Dr. Li is a shareholder and director of the Company and director of Tat Lung Hong Kong.

The amounts due from these related companies are unsecured, interest free, and have no fixed terms of repayment.

24. DEPOSITS WITH BANKS

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.

25. TRADE AND OTHER PAYABLES

	The Group		The Company	
	2003 $'000	2002 $'000	**2003 $'000**	2002 $'000
Trade payables	**9,379**	3,198	**–**	–
Other payables and accrued liabilities	**39,392**	12,588	**2,980**	2,044
	48,771	15,786	**2,980**	2,044

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	
	2003 $'000	2002 $'000
Due within 3 months or on demand	**9,379**	3,198

26. AMOUNTS DUE TO RELATED COMPANIES

	The Group	
	2003 $'000	2002 $'000
Everblooming Enterprises Company ("Everblooming")	**893**	897
Innova	**385**	–
	1,278	897

The amounts due to these related companies are unsecured, interest free, and have no fixed terms of repayment.

27. AMOUNT DUE TO A DIRECTOR

The amount outstanding at 31 December 2002 was unsecured, interest free and had no fixed terms of repayment. It was settled during the year.

28. INCOME TAX IN THE BALANCE SHEET

Current taxation in the consolidated balance sheet represents:

	The Group	
	2003 $'000	2002 $'000
Provision for taxation:		
Hong Kong	**–**	–
Outside Hong Kong	**12,660**	10,212
	12,660	10,212

29. SHARE CAPITAL

	2003		2002	
	No of shares '000	**Amount $'000**	No of shares '000	Amount $'000
Authorized:				
Ordinary shares of $0.01 each	**2,000,000**	**20,000**	2,000,000	20,000
Issued and fully paid:				
At 1 January	**835,000**	**8,350**	800,000	8,000
Shares issued under placement of shares	**–**	**–**	35,000	350
At 31 December	**835,000**	**8,350**	835,000	8,350

30. RESERVES

(a) The Group

	General reserve $'000	Share premium $'000	Contributed surplus $'000	Retained profits $'000	Exchange reserves $'000	Total $'000
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
At 1 January 2003	5,783	70,733	5,265	44,433	(12)	126,202
Loss for the year	–	–	–	(21,316)	–	(21,316)
Exchange difference	–	–	–	–	(393)	(393)
At 31 December 2003	**5,783**	**70,733**	**5,265**	**23,117**	**(405)**	**104,493**

(b) The Company

	Share premium $'000	Contributed surplus $'000	Accumulated losses $'000	Total $'000
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
At 1 January 2003	70,733	5,265	(5,516)	70,482
Loss for the year	–	–	(5,683)	(5,683)
At 31 December 2003	**70,733**	**5,265**	**(11,199)**	**64,799**

30. RESERVES (continued)

(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 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. No such appropriations have been made during the relevant year.

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 statuory financial statements, to an enterprise 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.

(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 $27,000 (2002: $15,000), being the accumulated losses attributable to an associate.

(h) At 31 December 2002 and 2003, the Company had no reserve available for distribution to shareholders.

31. COMMITMENTS

(a) Capital commitments

Capital commitments in respect of capital contribution to the subsidiaries, land, buildings, and plant and machineries outstanding at 31 December 2003 not provided for in the financial statements were as follows:

Contracted for:

	The Group		The Company	
	2003 $'000	2002 $'000	2003 $'000	2002 $'000
Capital contributions to the subsidiaries	11,700	32,292	–	32,292
Land, buildings and plant and machineries	–	5,415	–	–
	11,700	37,707	–	32,292

(b) Operating lease commitments

At 31 December 2003, the total future minimum lease payments under non-cancellable operating leases in respect of land and buildings are payable as follows:

	The Group	
	2003 $'000	2002 $'000
Within 1 year	665	112

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.

32. 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.

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 separatively 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) of the financial statements.

33. 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.

34. RELATED PARTY TRANSACTIONS

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

	Note	2003 $'000	2002 $'000
Innova	(i)		
– Sale of medical equipment and accessories		519	–
– Purchase of medical equipment and accessories		323	–
Li Hoi Yin	(ii)	169	–
Advance to Innova		–	408
Advance to Wuzhou Tat Lung	(iii)	75	–
Advance from Innova	(iv)	384	–
Advance from a director		–	888

Notes:

(i) Innova is a minority shareholder of Sino-Innova. During the year Sino-Innova sold certain medical equipment and accessories totalling $519,000 to and purchased certain medical equipment and accessories totalling $323,000 from Innova.

(ii) During the year ended 31 December 2003, the Group leased an office premise from Ms Li Hoi Yin, who is the wife of Mr Xu Xin. Mr Xu is the General Manager of Sino-Innova.

(iii) During the year ended 31 December 2003, the Group advanced to Wuzhou Tat Lung, a related party, an amount of $75,000 (2002: Nil). The advance is interest free, unsecured and has no fixed repayment terms.

(iv) During the year ended 31 December 2003, the Group borrowed from Innova, an amount of $384,000 (2002: Nil). The borrowing is interest free, unsecured and has no fixed repayment terms.

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.

Four Years' Summary

(Expressed in Hong Kong dollars)

	2000 $'000	2001 $'000	2002 $'000	**2003 $'000**
Results				
Turnover	11,017	38,523	49,850	**33,937**
Profit/(loss) from operations	5,966	26,936	27,987	**(18,736)**
Finance costs	(137)	(316)	–	**(136)**
Share of loss of an associate	–	–	(15)	**(12)**
Profit/(loss) from ordinary activities before taxation	5,829	26,620	27,972	**(18,884)**
Income tax	(995)	(4,217)	(4,993)	**(2,445)**
Profit/(loss) after taxation	4,834	22,403	22,979	**(21,329)**
Loss shared by minority interests	–	–	–	**13**
Profit/(loss) attributable to shareholders	4,834	22,403	22,979	**(21,316)**
Assets and liabilities				
Fixed assets	19,053	22,420	22,608	**24,243**
Construction in progress	–	–	1,547	**825**
Intangible assets	–	–	–	**58,537**
Negative goodwill	(14,588)	(11,706)	(8,824)	**(5,943)**
Interest in an associate	–	–	447	**435**
Net current assets	5,841	81,629	118,774	**38,808**
Non-current liabilities	(5,455)	–	–	**–**
Minority interests	–	–	–	**(4,062)**
NET ASSETS	4,851	92,343	134,552	**112,843**
Share capital	10	8,000	8,350	**8,350**
Reserves	4,841	84,343	126,202	**104,493**
	4,851	92,343	134,552	**112,843**
Earnings/(loss) per share (in Hong Kong cents)				
Basic	1.05	4.34	2.82	**(2.55)**
Diluted	0.95	3.45	N/A	**N/A**