

CHINA MEDICAL SCIENCE LIMITED
中華藥業有限公司*

(Incorporated in the Cayman Islands with limited liability)

ANNUAL REPORT
2004

** For identification purposes only*

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

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Corporate Information

EXECUTIVE DIRECTORS

Wong Sai Chung (*Chairman*)
Wong Sai Wa
Kwan Kai Cheong
Dr. Tang Gang
Wong Fei Fei

INDEPENDENT NON-EXECUTIVE DIRECTORS

Chow Wai Ming
Lai Chik Fan
Garry Alides Willinge

AUDIT COMMITTEE

Chow Wai Ming
Lai Chik Fan
Garry Alides Willinge

COMPLIANCE OFFICER

Kwan Kai Cheong

COMPANY SECRETARY

Yu Ling Ling, *ACIS, ACS*

QUALIFIED ACCOUNTANT

Hui Hok Sun, *ACCA, CPA (HKICPA)*

PRINCIPAL BANKERS

The Agricultural Bank of China, PRC
Bank of China (Hong Kong) Limited
Bank of China, PRC
Bank of Communications, PRC
Citic Industrial Bank, PRC
Industrial and Commercial Bank of China, PRC

REGISTERED OFFICE

Ugland House
P.O.Box 309
George Town
Grand Cayman
Cayman Islands
British West Indies

AUDITORS

PKF
Certified Public Accountants

HEAD OFFICE AND PRINCIPAL PLACE OF BUSINESS IN HONG KONG

14th Floor, Wheelock House
20 Pedder Street
Central
Hong Kong

PRINCIPAL SHARE REGISTRAR AND TRANSFER AGENT

Bank of Butterfield International (Cayman) Ltd.

HONG KONG BRANCH SHARE REGISTRAR AND TRANSFER OFFICE

Tengis Limited
G/F., Bank of East Asia Harbour View Centre
56 Gloucester Road
Wanchai, Hong Kong

Chairman's Statement

FINANCIAL REVIEW

Turnover for the year ended 31 July 2004 amounted to approximately HK\$171,533,000, which represented an increase of approximately 34.0% as compared with the preceding year. The increase is mainly attributable to the full year's turnover of Sichuan Shule being included as part of the Group's turnover for the year ended 31 July 2004. In the corresponding period in the preceding year, only two months of the turnover of Sichuan Shule was included in the Group's turnover in accordance with the timing of the Group's acquisition of Sichuan Shule. Intensified price competition in the infusion medicine and also the packaging materials market continued to be a significant factor impairing the turnover for the year under review. This caused a decrease in sale of infusion medicine by Chengdu Mt. Green and packaging materials by Sichuan Future of approximately 54.4% and approximately 52.4% respectively as compared with the previous year. Together with the substantial increase in provision for bad and doubtful debts, the Group recorded a loss for the year of approximately HK\$43,791,000 (2003: approximately HK\$652,000).

As the competition in the pharmaceutical industry being intensified and the outbreak of "SARS" epidemic in the PRC, the financial position of some of the Group's customers has deteriorated. In view of these unfavourable situation and considering the recoverability of its trade receivables, the Group adopted a prudent approach in that a provision for bad and doubtful debts of approximately HK\$20,204,000 was made for the year under review.

Segment information

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

It should be noted that within the Human Drugs segment, the operations of Sichuan Shule and an associate, Chengdu Mt. Green Li Kong Medical Technology Co. Ltd. ("Chengdu Mt. Green Li Kong"), were profitable, overall, however, the Human Drugs segment recorded a net loss for the year under review due to the losses of Chengdu Mt. Green.

Liquidity, financial resources and capital structure

The Group generally financed its operation through internally generated cashflows and banking facilities provided by its principal bankers in the PRC. As at 31 July 2004, the aggregate borrowings were approximately HK\$212,066,000 (31 July 2003: approximately HK\$223,135,000) of which approximately HK\$112,843,000 (31 July 2003: approximately HK\$111,265,000) were partially secured by pledged bank deposits or by assets of certain subsidiaries. As at 31 July 2004, the amount of banking facilities available and utilized was approximately HK\$300,894,000 (31 July 2003: approximately HK\$290,122,000). Except for the 3% Convertible Note, the Group's bank and other loans bear interest at the prevailing market rate.

Chairman's Statement

Liquidity, financial resources and capital structure *(continued)*

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

Gearing ratio

As at 31 July 2004, the gearing ratio (total borrowing, including notes payable, less cash and cash equivalents and pledged bank deposits to total assets) was approximately 39.0% (31 July 2003: approximately 36.9%).

Foreign exchange exposure

The Group mainly earns revenue and incurs cost in Renminbi. The Directors consider that the impact of foreign exchange exposure of the Group is minimal and, therefore, no hedging against foreign currency exposure is considered necessary.

Charges on group asset

As at 31 July 2004, leasehold land and buildings situated in the PRC, and plant and machinery with net book values of approximately HK\$64,413,000 (31 July 2003: approximately HK\$68,337,000), and HK\$29,290,000 (31 July 2003: approximately HK\$35,232,000) respectively and bank and time deposits of approximately HK\$65,649,000 (31 July 2003: approximately HK\$63,512,000) were pledged to secure general banking facilities granted to the Group.

Contingent liabilities

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

Commitments and significant investment

At 31 July 2004, the Group had outstanding capital commitment of approximately HK\$14,804,000 (31 July 2003: approximately HK\$4,943,000) and the Group did not have any significant investments during the year.

Future plan for investment

Except as disclosed in the financial statements, as at 31 July 2004, the Group did not have future plan for material investment and capital assets. However, as will be stipulated in the section "Outlook" below, in the event that a strategic alliance partner and/or one or more investors decide to join force with the Group, investment will be made in the construction of a GMP-compliant vaccine factory.

Chairman's Statement

Material acquisitions/disposals

During the year ended 31 July 2004, Chengdu Yuan Heng, a 91% owned subsidiary established in Chengdu, Sichuan, completed the legal procedure for acquisition of 四川利亨生物藥業有限公司 (formerly named as Sichuan Animal Medicine Factory) and also 四川裕利來福製藥有限公司, a 24.53% owned subsidiary was disposed for the year. Except that, the Group had no other material acquisitions or disposals of subsidiaries and affiliated companies during the year under review.

Employee information

As at 31 July 2004, the Group had 1,008 employees (2003: 1,047) in Hong Kong and PRC. The total remuneration to employees, including director's emoluments amounted to approximately HK\$8,312,000 (2003: approximately HK\$8,496,000). The Group remunerates its employees based on their performance, qualification, experience and the prevailing industry practice. Other benefits include contributions to statutory mandatory provident fund scheme and medical coverage to its employees in Hong Kong and the statutory central pension schemes to its employees in the PRC.

Sichuan Shule Pharmaceutical Joint Stock Company Limited ("Sichuan Shule")

Compared with the two month's turnover of approximately HK\$13,130,000 included in the consolidated turnover of the Group for the year ended 31 July 2003, the turnover of Sichuan Shule was increased to approximately HK\$103,926,000 for the year under review. The improvement in the company's result was largely attributable to the efforts made by the management and the staff that have helped to expedite the pace of business development of the company. Moreover, timely adjustment to marketing strategies and product mix was made by the company to cope with the changes of pharmaceutical market.

In view of the competition in the pharmaceutical market being increasingly intensified, Sichuan Shule during the year under review continued to push on the research and development of new products. The company also continued its relentless efforts in optimising its production processes, strengthening of quality control process, and minimizing overall production costs.

The modification for the polypropylene bottle production line was completed and production permit was obtained from the State Food & Drug Administration ("SFDA") in September 2003. Also the technical modification of solid medicine workshop in compliance with the regulation of SFDA was completed and GMP certification was obtained from SFDA in June 2004. The company believes, with the completion of GMP modification on solid medicine workshop, the productivity of solid medicine workshop will be further enhanced and the product mix of Sichuan Shule optimised. Sichuan Shule made a positive contribution to the bottom line of the Group.

Chairman's Statement

Chengdu Mt. Green Pharmaceutical Co., Ltd. (“Chengdu Mt. Green”)

During the year under review, the turnover of Chengdu Mt. Green amounted to approximately HK\$25,130,000, representing a decrease of approximately 54.4% as compared with the turnover for the preceding year. There are three major reasons for the decrease. Firstly, the regulatory changes introduced by SFDA intensified the adjustment of industry structure and market competition of the infusion medicine industry, causing downward price changes. Secondly, due to fierce market competition, in order to gain market shares, most of the competing manufacturers have reduced the selling prices of their products. The absolute amount of sales was then reduced, and almost emptied the profit margin. Moreover, the increase in the production costs on the manufacture and development of infusion medicine products, and double-fold increase in transportation cost during the year under review also caused a reduction in the profit margin thereof. In view of the decreasing profit margins of infusion medicine, Chengdu Mt. Green reduced its overall production during the year under review and shifted its efforts towards products with higher profit margin.

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

Sichuan Future recorded a turnover of approximately HK\$17,524,000 for the year under review, representing a decline of approximately 52.4% as compared with that of 2003. The decrease was mainly due to the following factors: (1) The price competition in the infusion medicine market becomes increasingly fierce, which put greater pressure on the demand of medical cap, and also its selling price. (2) Currently, the policy on GMP certification is not strictly imposed by the State, enabling small-scale irregular manufacturers to dump their products in the market. (3) 28f series of medical cap with low profit margin was and still is one of major risk factors for Sichuan Future's performance. Concurrently, a large increase in the plastic and aluminium costs on the manufacture of medical cap and increase in transportation cost during the year under review also caused the overall profit margin to be weighed down. Facing with such unfavourable market conditions, Sichuan Future gradually reduced its production of low end products and transformed its production to high end products in order to reduce its reliance currently placed on the infusion medicine market. However, as the product transformation is still in its early phase, it was inevitable that the sale volume of the company for the year under review was lower when compared with the preceding year.

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

Yuan Heng recorded a turnover of approximately HK\$23,209,000 during the year under review, which was approximately the same as the turnover recorded in the preceding year. There are two major factors affecting the performance for the year. Firstly, the regulatory change on packaging of veterinary drugs by the Ministry of Agriculture, which caused products in old packing be returned for re-packaging. As a result, Yuan Heng suffered loss on the repackaging of products and slowed down overall production schedule for the year under review. Secondly, price competition from small non-GMP compliant manufacturers was fierce. This caused Yuan Heng to reduce the selling price of 8% on average of its products for the year under review.

Chairman's Statement

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

The legal procedures for the acquisition of 四川利亨生物藥業有限公司 (formerly named as Sichuan Animal Medicine Factory) were all completed in December 2003, the production permit and the approval for transferring 18 vaccines to 四川利亨 was also obtained from the relevant authority in December 2003. The directors believe that the acquisition of 四川利亨 will further enhance the overall competitiveness of the Group and better position the company in the veterinary drug industry. The turnover of approximately HK\$1,744,000, representing seven month's sale of 四川利亨 since the acquisition, was included as part of the turnover of the Group for the year ended 31 July 2004.

Research and Development

Human drug:

The major research and development projects undertaken by Sichuan Shule are currently progressing well. During the year under review, two products have obtained the production permit from SFDA, namely Glucose and Sodium Chloride Potassium Chloride Injection, Ribavirin and Glucose Injection. The result in respect of pre-clinical test for certain new drugs under categories I and III were also reported to SFDA for drug supervision.

Veterinary drug:

During the year under review, 25 products had obtained pharmaceutical registration, namely Enrofloxacin for injection, Doxycycline Hyclate for injection, Compound Gentamycini-micronomicini Sulfatis Injection, Estradiol Benzoate Injection, Compound Ciprofloxacin Hydrochloride-II Injection, Shuanghuanglian Zhusheyeye, Compound Herba Senecionis Scandentis Injection, Compound Ciprofloxacin Hydrochloride Injection, Spectinomycin Hydrochloride and Lincomycin Hydrochloride Injection, Compound Thiamphenical Injection, Compound Kanamycin Sulfate Suspension Injection, Compound Amikacin Sulfate Injection, Ketoprofen Injection, Compound Sulfamonomethoxine Sodium Longacting Injection, Compound Bulbus Allii Injection, Compound Radix Isatidis Injection, Compound Tylosin Injection (5ml), Compound Tylosin Injection (10ml), Florfenicol Injection, Shuang Ding Zhusheyeye, Compound Amoxicillin Sodium for Injection, Erythromycin Lactobionate for Injection, Ofloxacin and Diprophylline Injection, Compound Bethanechol Chloride Injection and Ampicillin Sodium for Injection.

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

OUTLOOK

The research and development of new products will be the key tasks for Sichuan Shule in the year of 2004. Capitalizing on Sichuan Shule's experience in the manufacturing of nutritional infusion medicines, the company will further enlarge its production scale of more new products under the categories of Fat Emulsion, Profpofol and Bambuterori Hydrochloride Capsules, thereby strengthening the company's favourable position in the market. Sichuan Shule and Chengdu Mt. Green Li Kong are the only two business entities within the Human Drugs segment that are profitable. We will focus on the development of these two entities. With regard to the loss making Chengdu Mt. Green business, the directors are making serious review of its operation and will take immediate corrective measures to ensure that it will no longer impact negatively the profitability of the Group.

At the same time, as Sichuan Future continues to make loss, the directors are taking similar action as that for Chengdu Mt. Green to ensure that it does not impose a continuing negative impact to the profitability of the Group.

As the development of modernized agriculture and husbandry industry becomes one of the prime directives of the PRC government, it is evident that demand for modern vaccine products of international standards is growing in intensity. Chengdu Yuan Heng holds one of the 28 vaccine production licenses in the PRC. The directors believe in the huge potential of this business and are in discussion with potential strategic partners in the industry and investors with the view of investing together on the construction of a new GMP-compliant vaccine factory to take advantage of this huge and potentially highly profitable segment of the market.

Profiles of Directors and Senior Management

EXECUTIVE DIRECTORS

Mr. Wong Sai Chung, aged 54, is one of the founders of the Group and is responsible for the overall policy and management of the Group. He is a director and sole shareholder of Seechain (prior to the group reorganisation for the purpose of listing), which invested in Sichuan Future, Chengdu Mt. Green and Chengdu Yuan Heng. After working in the management of various family businesses, Mr. Wong founded the Pacific Concord Group in 1982. He has over 20 years of experience in corporate management. Mr. Wong is also the Chairman and Joint Managing Director of Pacific Concord Holding Limited (a listed company on the Main Board of the Stock Exchange and was privatised in October 2003) since 1987. He is a brother of Mr. Wong Sai Wa.

Mr. Wong Sai Wa, aged 61, is one of the founders of the Group and is responsible for formulating the strategy and overseeing the development of the Group. Mr. Wong holds a degree in Mechanical Engineering from the Scientific and Engineering University in the PRC and completed the Stanford Executive Program in 1993. Mr. Wong is also a Director of Pacific Concord Holding Limited since 1987 and was appointed as a Joint Managing Director since 1999. He is a brother of Mr. Wong Sai Chung and the father of Mr. Wong Fei Fei.

Mr. Kwan Kai Cheong, aged 54, is responsible for general management and strategic alliance relationship of the Group. Mr. Kwan is also a Director of Pacific Concord Holding Limited since 1993 and was appointed as a Joint Managing Director since 1999. Prior to joining the Pacific Concord Group, he was the President for the Asia Pacific Region of Merrill Lynch & Co., Mr. Kwan graduated from the University of Singapore with a degree in Accounting and is qualified as a Chartered Accountant in Australia. He completed the Stanford Executive Program in 1992. Mr. Kwan was appointed as director in September 2000.

Mr. Kwan has been actively involved in the financial planning underlying the formation of the Group, the establishment of the accounting and reporting system for each of the operating subsidiaries of the Group, namely Sichuan Future, Chengdu Mt. Green and Chengdu Yuan Heng, to ensure the smooth and effective operation of the companies and the implementation of the initial public offering exercise.

Dr. Tang Gang, aged 56, is the general manager and one of the founders of Sichuan Future. He is responsible for the daily operations of the Group. Dr. Tang is a registered doctor in the PRC and graduated from Chongqing Medical University (重慶醫科大學). After graduation, Dr. Tang practiced and held various senior positions in the management of hospitals for many years. Prior to setting up Sichuan Future in 1997, Dr. Tang was director of various companies and has years of experience in corporate management. Dr. Tang was appointed as director in September 2000.

He is currently responsible for the daily operations of the Group as well as supervising the setting of GMP standard for production facility of packaging materials for pharmaceutical products in the PRC. Dr. Tang indirectly holds 4.5 per cent. interest in Sichuan Future.

Mr. Wong Fei Fei, aged 30, is responsible for general management. Mr. Wong obtained a Simultaneous Bachelor of Arts degree in Economics and Dramatic Arts (honours) from University of California, Berkeley. Mr. Wong was awarded the Roselyn Schneider Eisner Price, the highest honour for students in the creative arts from University of California, Berkeley. Since graduation he has worked at Dantz Development Inc., a software development company in Silicon Valley. Mr. Wong is the son of Mr. Wong Sai Wa. Mr. Wong was appointed as a director in September 2000.

Profiles of Directors and Senior Management

INDEPENDENT NON-EXECUTIVE DIRECTORS

Mr. Tsim Tak-Lung, Dominic, aged 57, joined the Group in September 2000. He is also a non-executive director and the vice chairman of Playmates Toys Holdings Limited and a non-executive director of Far Eastern Polychem Industries Limited. He is also the chairman of New-Alliance Asset Management (Asia) Ltd. He operates his own consultancy business, advising multi-national companies on risk management and strategic planning. Mr. Tsim is very active in various community services in Hong Kong. He is a Justice of the Peace and has served two terms on the Central Policy Unit of the Hong Kong Government. He also serves as a trustee of Shaw College of The Chinese University of Hong Kong. Mr. Tsim was appointed as a director in September 2000. He resigned due to personal reason in October 2004.

Mr. Chow Wai Ming, aged 50, graduated from University of Hong Kong. Mr. Chow has over 20 years of investment banking experience including 15 years at Schroders Asia Ltd., one of the largest investment banks and fund managers in Europe. In 1999, he was the Vice Chairman of the Hong Kong Capital Markets Association (the "Association") whose objective is to promote the local debt capital markets. The Association has over 100 active investment banks as its members. Mr. Chow was also the convenor of the Association's PRC sub-committee from 1995 to 2000. Mr. Chow was appointed as a director in July 2003.

Mr. Chow is also the financial advisor of the Tianjin Municipal government where he advises the Tianjin Municipal government in relation to the development of the Tianjin new coastal area.

Mr. Garry Alides Willinge, aged 54, is a fellow of the Australian Institute of Company Directors. He graduated with a Diploma of Finance and Investment from the Securities Institute of Australia in 1992. Mr. Willinge is currently a Director, Global Services, IBM China/Hong Kong Ltd. He has previously worked in a number of IBM Asia Pacific business unit leadership roles. This includes Director of Asia Pacific Business Development, responsible for forging alliances and joint ventures across Asia to grow IBM's services portfolio. He was also Director, Information Technology, Sydney Olympic Games 2000. He has extensive external experiences and commitments. He was assigned to the West Australian Premier in 1990, where he led the Office of Public Sector Management, focused on leading public sector reform and transforming CEO leadership in the public sector. In Hong Kong, he is appointed to the General Management Committee of the Hong Kong Management Association. Mr. Willinge was appointed as a director in September 2004.

Mr. Lai Chik Fan, aged 56, is a seasoned investment banker with over 25 years' experience in the industry. He is known for his integrity and his years of experience in the area of equities sales and distribution. Mr. Lai is currently a partner of AR Evans Capital Limited. In the past, he had held senior positions with international investment banks and he was previously Managing Director of Merrill Lynch (Asia Pacific) Ltd, Smith Barney (Hong Kong) Ltd, and Chin Tung Securities Ltd. Mr. Lai was appointed as a director in October 2004.

Profiles of Directors and Senior Management

INTERNATIONAL ADVISORY COMMITTEE

In order to formulate strategies suitable for the future development of the Group, the Group has invited the following experts to form an International Advisory Committee.

Mr. Song Rui Lin, aged 41, has years of experience and expertise in formulating regulations and policies for the pharmaceutical industry in the PRC. Mr. Song is a fellow of the Chinese Medical Association, a member of the PRC Law Association and he is also a member of the National Chinese Drugs Protection and Assessment Committee.

Mr. Lee Tak Foo, aged 48, has years of experience and expertise in the field of biotechnology products. Since 1967, Mr. Lee has been involved in the research for various viruses using live cells. Between 1994 and 1999, he was the deputy head of the PRC Biotechnology and Pharmaceutical Products Laboratory. Mr. Lee is now the secretary and deputy officer of (中國生物製品標準委員會), a member of (中國醫學學會), the deputy chairman of (中國微生物學會), a general officer of (中國醫藥生物技術協會), and a committee member of (國家藥典委員會), National Committee on the Assessment of New Medicinal Products (國家新藥審評委員會) and a member of the State Drug Administration (國家藥品監督員) respectively.

Dr. Xiao Min (肖敏), aged 45, has years of experience and expertise in the field of biomedical research. Since 1990, Dr. Xiao has conducted numerous “cutting-edge” research projects at Harvard Medical School, and Millennium Pharmaceuticals, Cambridge, Massachusetts. Dr. Xiao has been conducting genetic research to develop drugs that effectively treat cancers, pain, and inflammatory diseases. Dr. Xiao’s expertise in the tissue-engineering technology has far-reaching clinical applications.

Dr. Liu Zhi Min, aged 44, has years of experience and expertise in the field of genetic biotechnology engineering. He is now a committee member of (中國全軍醫學技術委員會生物工程專業員會), (中國生物工程學會) and (中國全軍醫學科學院生物工程研究所學術委員會), and (中國全軍醫藥評審專家) respectively.

Professor Zhang Si Liang, aged 61, has years of experience and expertise in the field of bio-chemical engineering. He is now an officer of National Biochemical Engineering Research Centre (Shanghai) (國家生化工程技術研究中心(上海)), the deputy dean of biotechnology engineering faculty of the Huadong Polytechnic University (華東理工大學生物工程學院), a committee member of (中國生物工程學會) and (中國微生物學會) respectively, and an editorial committee member of (中國醫藥工業雜誌).

Dr. Chu Ju, aged 40, has years of experience and expertise in the field of microbiology. Dr. Chu has been engaged in the research of micro organism in Japan since 1990 and a number of biotechnology projects in the US. Dr. Chu is now a committee member of (中國生物工程學會) and (國際腦研究組織) respectively.

Profiles of Directors and Senior Management

SENIOR MANAGEMENT

Mt. Green Li Kong

Ms. Xu Shi Lan, aged 50, is the general manager of Mt. Green Li Kong Co. Ltd. (青山利康藥業有限公司) and holds a position as an associate researcher. She holds a master degree in law of Sichuan University. Ms. Xu acted as officer and other key positions in a medical university and vice general manager in a pharmaceutical company. Ms Xu has 20 years of experience in corporate management.

Mr. Li Yun Tian, aged 40, is the financial controller of Mt. Green Li Kong Co. Ltd. (青山利康藥業有限公司) and holds a position as an accountant. He is graduated in professional accounting field. Mr. Li worked in the First Subsidiary Hospital of Wa Xi University (華西醫科大學) as a chief financial controller of the State Chinese Medicine Safety Assessment Centre. Mr. Li has profound experience in finance.

Medical Section

Mr. Wang Ya Jun, aged 39, is the deputy general manager of the Group's medical section. Mr. Wang is a chief pharmaceutical engineer and holds a master degree in business administration of Sichuan University. He has nearly 20 years of experience in pharmaceutical enterprise technology and production management. Since 1985, he has been working in the corporate of Sichuan Shule (四川蜀樂). He was promoted deputy general manager of the company.

Dr. Shao Jian Ben, aged 62, is the deputy general manager of the Group's medical section. Dr. Shao manages the doctors. He holds a master degree in combined Speciality of organic medicine of Second Military Medical University. He has served in military hospital for years and is experienced in the R&D management of pharmaceutical enterprise.

Ms. Yu Qiong Qiong, aged 52, is the financial controller of the Group's medical section and is responsible for the accounting functions of Sichuan Future. She is a certified public accountant in the PRC and graduated from the accounting of South West Finance University (西南財經大學). Ms. Yu has years of experience in finance and accounting. Ms Yu is the wife of Dr. Tang Gang, an executive director of the Group.

Ms. Huang You Qin, aged 56, is the vice financial controller of the Group's medical section. Ms. Huang graduated from the Accounting field of South West Finance University (西南財經大學) and is a senior accountant with full experience in financial management and accounting in large enterprises.

Mr. Zhang Yue, aged 41, is the head of the Supply Department of the Group's medical section and the general manager of Sichuan Future. Prior to joining the Group, he worked in Chengdu Railway Bureau (成都鐵路局) for 15 years. He graduated from Sichuan Technology University (四川科技大學).

Profiles of Directors and Senior Management

SENIOR MANAGEMENT (continued)

Medical Section (continued)

Ms Yuan Cheng Gao, aged 54, is the head of the R&D department of the Group's medical section and the head of the quality control department of Sichuan Shule (四川蜀樂). Ms Yuan is a pharmaceutical engineer with specialty qualification of the Pharmaceutical Faculty of Chengdu Chinese Medicine University. She has worked in hospitals before and has more than 20 years of experience in the examination, quality inspection, quality control, R&D of drugs in pharmaceutical enterprise, as well as work experience in the middle-ranks.

Veterinary Drug Section

Mr. Xiong Nan, aged 58, is the general manager of the Group's Veterinary drug section. He graduated from Advance Learning Institute of Economic Management for Civil Servants in Chengdu (成都經濟管理幹部進修學院) as an economist in 1992. He has years of experience in management.

Mr. Dai Yong De, aged 37, is the deputy general manager of the Group's veterinary drug section. He graduated from Jiangsu Animal Husbandry College (江蘇省畜牧獸醫藥專校) with a diploma on veterinary drugs (獸藥專業課程) in 1988. He has years of experience in the research and development in veterinary drugs.

Mr. Shi Mei Qi, aged 44, is the head of the sales department of the Group's veterinary drug section. Mr. Shi is an economist and holds a MBA degree of Economic and Management Institute in Sichuan Province (四川省經濟管理學院). He has worked in large military and industrial enterprises and has 8 years of experience in sale management of veterinary drugs.

Mr. Li Hua Liang, aged 40, is the financial controller of the Group's Veterinary Drug section. Mr. Li is a registered accountant graduated from Anhui University of Finance and Trade (安徽財貿大學) and has profound experience in financial management of sizable integrated companies.

Hong Kong

Ms. Hui Hok Sun, aged 37, is the qualified accountant of the Company. She is a member of both the Association of Chartered Certified Accountants and Hong Kong Institute of Certified Public Accountants with more than 10 years experience in the accounting field.

Ms. Yu Ling Ling, aged 39, is the company secretary of the Company and Manager of the Company Secretarial Department of Pacific Concord Holding Limited. She is an associate member of The Institute of Chartered Secretaries and Administrators and The Hong Kong Institute of Company Secretaries. Ms. Yu joined the Group in May 2000.

Use of Proceeds from the Placing of New Shares

From the date of listing on 10 April 2001, the Group invested approximately HK\$4.3 million, HK\$20.4 million, HK\$18 million and HK\$1.5 million on various projects in the financial years ended 2001, 2002, 2003, and 2004 respectively. The use of proceeds for the year ended 31 July 2004 was mainly used for the purchase of production equipment.

Report of the Directors

The directors have pleasure in presenting their annual report together with the audited financial statements of the Company and the Group for the year ended 31 July 2004.

PRINCIPAL ACTIVITIES

The principal activity of the Company is investment holding. Details of the principal activities of the subsidiaries are set out in note 16 to the financial statements. There were no significant changes in the nature of the Group's principal activities during the year.

RESULTS AND DIVIDENDS

The Group's loss for the year ended 31 July 2004 and the state of affairs of the Company and the Group at that date are set out in the financial statements on pages 25 to 70.

The directors do not recommend the payment of any dividend in respect of the year ended 31 July 2004.

Report of the Directors

FINANCIAL SUMMARY

A summary of the results and of the assets, liabilities and minority interests of the Group for the five financial periods ended 31 July 2004 is set out below:

RESULTS

	Year ended 31 July 2004 HK\$'000	Year ended 31 July 2003 HK\$'000	Year ended 31 July 2002 HK\$'000	Year ended 31 July 2001 HK\$'000	Period from 25 June 1999 to 31 July 2000 HK\$'000
Turnover	<u>171,533</u>	<u>128,046</u>	<u>180,925</u>	<u>184,045</u>	<u>25,089</u>
(Loss)/profit from operating activities	<u>(30,365)</u>	<u>9,152</u>	<u>33,361</u>	<u>39,226</u>	<u>2,611</u>
Finance costs	<u>(14,555)</u>	<u>(9,415)</u>	<u>(9,520)</u>	<u>(7,081)</u>	<u>(1,432)</u>
Share of results of an associate	<u>1,449</u>	<u>(1,202)</u>	<u>(272)</u>	<u>–</u>	<u>–</u>
(Loss)/profit before tax	<u>(43,471)</u>	<u>(1,465)</u>	<u>23,569</u>	<u>32,145</u>	<u>1,179</u>
Tax expense	<u>(337)</u>	<u>(783)</u>	<u>(848)</u>	<u>–</u>	<u>–</u>
(Loss)/profit before minority interests	<u>(43,808)</u>	<u>(2,248)</u>	<u>22,721</u>	<u>32,145</u>	<u>1,179</u>
Minority interests	<u>17</u>	<u>1,596</u>	<u>(2,223)</u>	<u>(3,051)</u>	<u>(504)</u>
(Loss)/profit attributable to shareholders	<u>(43,791)</u>	<u>(652)</u>	<u>20,498</u>	<u>29,094</u>	<u>675</u>

(Note a)

ASSETS, LIABILITIES AND MINORITY INTERESTS

	31 July				
	2004 HK\$'000	2003 HK\$'000 (Restated)	2002 HK\$'000	2001 HK\$'000	2000 HK\$'000
TOTAL ASSETS	<u>584,140</u>	<u>590,169</u>	<u>416,104</u>	<u>316,602</u>	<u>157,800</u>
TOTAL LIABILITIES	<u>(497,159)</u>	<u>(454,399)</u>	<u>(286,675)</u>	<u>(203,572)</u>	<u>(124,189)</u>
MINORITY INTERESTS	<u>(11,036)</u>	<u>(16,034)</u>	<u>(9,041)</u>	<u>(13,140)</u>	<u>(32,911)</u>
	<u>75,945</u>	<u>119,736</u>	<u>120,388</u>	<u>99,890</u>	<u>700</u>

(Note b)

Report of the Directors

Note:

- (a) *The results of the Group for the period ended 31 July 2000 have been prepared on a combined basis as if the current group structure had been in existence throughout the period and have been extracted from the Company's prospectus dated 28 March 2001.*
- (b) *The effect of adopting SSAP 12 (revised) has been adjusted to the opening balances of deferred taxation and goodwill as at 1 August 2003.*

FIXED ASSETS

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

SHARE OPTIONS

Details of the Company's share option schemes are set out in note 29 to the financial statements.

PRE-EMPTIVE RIGHTS

There are no provisions for pre-emptive rights under the Company's bye-laws or the laws of the Cayman Islands which would oblige the Company to offer new shares on a pro-rata basis to existing shareholders.

PURCHASE, REDEMPTION OR SALE OF LISTED SECURITIES OF THE COMPANY

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

RESERVES

Details of movements in the reserves of the Company and the Group during the year are set out in note 30 to the financial statements and in the consolidated statement of changes in equity on page 31, respectively.

DISTRIBUTABLE RESERVES

As at 31 July 2004, the Company's distributable reserves amounted to HK\$49,468,000.

Report of the Directors

MAJOR CUSTOMERS AND SUPPLIERS

Sales to the Group's five largest customers accounted for 80% of the total sales for the year and sales to the largest customer included therein amounted to 75%. Purchases from the Group's five largest suppliers accounted for 33% of the total purchases for the year and purchases from the largest supplier included therein amounted to 16%.

None of the directors of the Company or any of their associates or any shareholders (which, to the best knowledge of the directors, own more than 5% of the Company's issued share capital) had any beneficial interest in any of the Group's five largest customers and suppliers.

DIRECTORS AND DIRECTORS' SERVICE CONTRACTS

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

Executive directors:

Mr. Wong Sai Chung (*Chairman*)

Mr. Wong Sai Wa

Mr. Kwan Kai Cheong

Dr. Tang Gang

Mr. Wong Fei Fei

Independent non-executive directors:

Mr. Chow Wai Ming

Mr. Garry Alides Willinge (Appointed on 28 September 2004)

Mr. Lai Chik Fan (Appointed on 21 October 2004)

Mr. Tsim Tak Lung, Dominic (Resigned on 21 October 2004)

In accordance with article 99 of the Company's Articles of Association, Mr. Garry Alides Willinge and Mr. Lai Chik Fan will retire by rotation and, being eligible, offer themselves for re-election at the forthcoming annual general meeting.

In accordance with article 116 of the Company's Articles of Association, Mr. Wong Sai Wa and Mr. Kwan Kai Cheong will retire by rotation and, being eligible, offer themselves for re-election at the forthcoming annual general meeting.

Report of the Directors

DIRECTORS AND DIRECTORS' SERVICE CONTRACT *(continued)*

Mr. Wong Sai Wa and Mr. Kwan Kai Cheong, both are the executive directors of the Company since 27 September 2000. Mr. Garry Alides Willinge and Mr. Lai Chik Fan, both are the independent non-executive directors of the Company appointed on 28 September 2004 and 21 October 2004 respectively. Details of their previous experience can be referred to the section "Profiles of Directors and Senior Management". Both Mr. Wong and Mr. Kwan have entered into a service contract with the Company as stipulated below. The remuneration for Mr. Wong is fixed at HK\$360,000 per annum whereas no remuneration has been received by Mr. Kwan. There is no service contract entered into between each of Mr. Willinge and Mr. Lai and the Company. Each of Mr. Willinge and Mr. Lai was appointed for a term of one year and the remuneration is HK\$120,000 per annum.

Save as disclosed under the section "Profiles of Directors and Senior Management", each of Messrs. Wong Sai Wa, Kwan Kai Cheong, Garry Alides Willinge and Lai Chik Fan does not have any relationship with any directors, senior management, management shareholders, substantial shareholders or controlling shareholders of the Company. As at the date hereof, save as disclosed under the section headed "Directors' and Chief Executives' Interests in Securities of the Company", each of Messrs. Wong Sai Wa, Kwan Kai Cheong, Garry Alides Willinge and Lai Chik Fan did not have any interests in the shares of the Company within the meaning of Part XV of the Securities and Futures Ordinance. Save as disclosed herein, the Board is not aware of any other matters which need to be brought to the attention of the shareholders of the Company.

Each of the executive directors has entered into a service contract with the Company for an initial terms of two years commencing from 10 April 2001 and shall be continuing thereafter, which is subject to termination by either party giving not less than six calendar months' written notice.

Mr. Garry Alides Willinge and Mr. Lai Chik Fan were each appointed for a term of one year with effect from 28 September 2004 and 21 October 2004 respectively. Mr. Chow Wai Ming is not appointed for specific terms. All independent non-executive directors are subject to retirement by rotation in accordance with the Company's Articles of Association.

Apart from the foregoing, no director proposed for re-election at the forthcoming annual general meeting has a service contract with the Company which is not determinable by the Company within one year without payment of compensation, other than statutory compensation.

DIRECTORS' AND SENIOR MANAGEMENT'S BIOGRAPHIES

Biographical details of the directors of the Company and the senior management of the Group are set out on pages 9 to 13 of the annual report.

DIRECTORS' INTERESTS IN CONTRACTS

Apart from the transactions as disclosed in note 36 to the financial statements, no other contracts of significance to which the Company or any of its holding companies or subsidiaries was a party and in which a director of the Company had a material interest subsisted at the end of the year or at any time during the year.

Report of the Directors

DIRECTORS' AND CHIEF EXECUTIVES' INTERESTS IN SECURITIES OF THE COMPANY

As at 31 July 2004, the interests or short positions of the directors and chief executives in the shares, underlying shares or debentures of the Company or any of its associated corporations (within the meaning of Part XV of the Securities and Futures Ordinance ("SFO")), which were notified to the Company and The Stock Exchange of Hong Kong Limited (the "Stock Exchange") pursuant to Divisions 7 and 8 of Part XV of the SFO (including interests or short positions which they have taken or deemed to have taken under such provisions of the SFO), or which were required, pursuant to Section 352 of the SFO, to be entered in the register referred to therein, or which were required, pursuant to Rules 5.46 to 5.67 of the GEM Listing Rules, to be notified to the Company and the Stock Exchange, were as follows:

Long positions in ordinary shares and underlying shares of the Company

Name of director	Capacity and nature of interest	Shares/equity derivatives	Number/amount of shares/equity derivatives held	Percentage of the Company's issued share capital	Note
Mr. Wong Sai Chung	Through controlled corporations	Ordinary shares	400,000,000 shares	80%	a
	Through controlled corporations	Convertible note	HK\$26,740,760	9.7%	b
Mr. Wong Sai Wa	Directly beneficially owned	Share options	3,200,000 share options	0.64%	c
Mr. Kwan Kai Cheong	Directly beneficially owned	Share options	3,000,000 share options	0.6%	c

Notes:

- (a) These shares are registered in the name of Concord Pharmaceutical Technology (Holdings) Limited ("CPT"), a wholly-owned subsidiary of Concord Business Management Limited ("CBM"). As at 31 July 2004, the entire issued share capital of CBM was owned by Mr. Wong Sai Chung. Accordingly, Mr. Wong Sai Chung is deemed to have an interest in the 400,000,000 shares of the Company held by CPT.
- (b) As at 31 July 2004, CPT held a convertible note (the "Convertible Note") with outstanding principal amount of HK\$26,740,760. The Convertible Note confers the right on CPT to convert such note into approximately 48,619,564 of the Company's new shares at an issue price of HK\$0.55 per share, representing approximately 9.7% of the issued share capital of the Company and approximately 8.9% of the issued share capital of the Company as enlarged by the shares which may fall to be issued on conversion. Mr. Wong Sai Chung has a beneficial interest in CPT as set out in note (a) above. Further details of the Convertible Note are set out in note 24 to the financial statements.
- (c) The details of the share options granted are set out in note 29 to the financial statements.

Report of the Directors

DIRECTORS' AND CHIEF EXECUTIVES' INTERESTS IN SECURITIES OF THE COMPANY

(continued)

Save as disclosed herein, as at 31 July 2004, none of the directors or chief executives has short positions in the shares or underlying shares of equity derivatives of the Company.

DIRECTORS' RIGHTS TO ACQUIRE SHARE OR DEBENTURES

Save as disclosed under the section headed "Directors' and Chief Executives' Interests in Securities of the Company" above, at no time during the year was the Company or any of its holding companies or subsidiaries a party to any arrangements to enable the Company's directors, their respective spouse or minor children to acquire benefits by means of the acquisition of shares in or debentures of the Company or any other body corporate.

SUBSTANTIAL SHAREHOLDERS' INTERESTS

As at 31 July 2004, the following persons (not being the directors and chief executives of the Company) had interests or short positions in the shares, underlying shares or debentures of the Company under the provisions of Divisions 2 and 3 of Part XV of the SFO, or which were recorded in the register required to be kept under Section 336 of the SFO as follows:

Long positions in ordinary shares and underlying shares of the Company

Name	Capacity and nature of interest	Shares/equity derivatives	Number/amount of shares/equity derivatives held	Percentage of the Company's issued share capital	Note
CPT	Directly beneficially owned	Ordinary shares	400,000,000 shares	80%	a and b
	Directly beneficially owned	Convertible note	HK\$26,740,760	9.7%	a and c
CBM	Through controlled corporation	Ordinary shares	400,000,000 shares	80%	a and b
	Through controlled corporation	Convertible note	HK\$26,740,760	9.7%	a and c

Notes:

- (a) CPT is a wholly-owned subsidiary of CBM. Accordingly, CBM is deemed to have interests in the 400,000,000 shares and convertible note of the Company held by CPT.
- (b) The shares held in the name of CPT are duplication of the shares held by the director, Mr. Wong Sai Chung.
- (c) The convertible note held by CPT is a duplication of the convertible note held by the director, Mr. Wong Sai Chung. Details of the convertible note are disclosed under the section headed "Directors' and Chief Executives' Interests in Securities of the Company" above.

Report of the Directors

SUBSTANTIAL SHAREHOLDERS' INTERESTS *(continued)*

So far as the directors are aware, save as disclosed herein, no persons (not being the directors and chief executives of the Company) have short positions in the shares or underlying shares of equity derivatives of the Company.

MANAGEMENT SHAREHOLDERS' INTERESTS

Save as disclosed under the sections headed "Directors' and Chief Executives' Interests in Securities of the Company" and "Substantial Shareholders' Interests" above, as at 31 July 2004, no other person was individually and/or collectively entitled to exercise or control the exercise of 5% or more of the voting power at general meeting of the Company and was able, as a practical matter, to direct or influence the management of the Company.

CONNECTED TRANSACTIONS

During the year, the Group had related party transactions as detailed in note 36 to the financial statements, which also constituted connected transactions under the GEM Listing Rules. In the opinion of the directors, such connected transactions were conducted in the normal course of business and the Company has complied with the relevant requirements under Chapter 20 of the GEM Listing Rules.

DIRECTORS' INTERESTS IN A COMPETING BUSINESS

None of the directors, the substantial shareholders or the management shareholders (as defined in the GEM Listing Rules) had any interests in any business which competed with or might compete with the business of the Group.

COMPLIANCE WITH RULES 5.34 TO 5.45 OF THE GEM LISTING RULES

The Company complied with the board practice and procedures as set out in Rules 5.34 to 5.45 of the GEM Listing Rules throughout the year ended 31 July 2004.

AUDIT COMMITTEE

The Company has an audit committee which was established with written terms of reference in compliance with the requirements as set out in rules 5.28 to 5.32 of the GEM Listing Rules. The duties of the audit committee are to review and to provide supervision over the financial reporting process and internal control system of the Group. The audit committee currently comprises three independent non-executive directors, namely Mr. Chow Wai Ming, Mr. Garry Alides Willinge and Mr. Lai Chik Fan.

Four audit committee meetings were held during the year ended 31 July 2004. The work undertaken by the audit committee was to review the company's quarterly, interim and annual financial reports and to provide advice and comments thereon to the board of directors.

Report of the Directors

AUDITORS

Subsequent to the balance sheet date, Messrs. Ernst & Young resigned and Messrs. PKF were appointed as the auditors of the Company.

A resolution to re-appoint the retiring auditors, Messrs. PKF, is to be proposed at the forthcoming Annual General Meeting.

On behalf of the Board

Wong Sai Chung

Chairman

Hong Kong

25 October 2004

Report of the Auditors

AUDITORS' REPORT TO THE SHAREHOLDERS OF CHINA MEDICAL SCIENCE LIMITED

(Incorporated in the Cayman Islands with limited liability)

We have audited the financial statements on pages 25 to 70 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.

It is our responsibility to form an independent opinion, based on our audit, on those statements and to report our opinion solely to you, as a body, 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 Institute of Certified Public 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 July 2004 and of the loss and cash flows of the Group for the year then ended and have been properly prepared in accordance with the disclosure requirements of the Hong Kong Companies Ordinance.

PKF

Certified Public Accountants

Hong Kong
25 October 2004

Consolidated Income Statement

For the Year ended 31 July 2004

	<i>Notes</i>	2004 HK\$'000	2003 HK\$'000
Turnover	5	171,533	128,046
Cost of sales		<u>(137,446)</u>	<u>(92,102)</u>
Gross profit		34,087	35,944
Other revenue and gains	5	4,833	2,268
Selling and distribution costs		(13,259)	(5,904)
General and administrative expenses		(17,186)	(12,196)
Other operating expenses		(18,636)	(8,801)
Provision for bad and doubtful debts		<u>(20,204)</u>	<u>(2,159)</u>
(Loss)/profit from operating activities	6	(30,365)	9,152
Finance costs	7	(14,555)	(9,415)
Share of results of an associate		<u>1,449</u>	<u>(1,202)</u>
Loss before tax		(43,471)	(1,465)
Tax expense	10(a)	<u>(337)</u>	<u>(783)</u>
Loss before minority interests		(43,808)	(2,248)
Minority interests		<u>17</u>	<u>1,596</u>
Loss attributable to shareholders	11	<u>(43,791)</u>	<u>(652)</u>
Loss per share	12		
Basic		<u>(8.76 cents)</u>	<u>(0.13 cents)</u>
Diluted		<u>N/A</u>	<u>N/A</u>

Consolidated Balance Sheet

As at 31 July 2004

	<i>Notes</i>	2004 HK\$'000	2003 HK\$'000 (Restated)
NON-CURRENT ASSETS			
Fixed assets	<i>13</i>	200,902	204,339
Intangible assets	<i>14</i>	12,428	9,485
Goodwill:	<i>15</i>		
Goodwill		20,088	17,731
Negative goodwill		(5,440)	(6,134)
Interest in an associate	<i>18</i>	9,583	8,134
Long term investments	<i>19</i>	4,420	4,420
Long term prepayments		–	5,405
Deferred tax asset	<i>10(b)</i>	257	–
		<u>242,238</u>	<u>243,380</u>
CURRENT ASSETS			
Inventories	<i>20</i>	21,470	28,535
Trade receivables	<i>21</i>	169,036	178,157
Deposits, prepayments and other receivables	<i>22</i>	42,178	30,831
Pledged deposits	<i>23</i>	65,649	63,512
Cash and cash equivalents	<i>23</i>	43,569	45,754
		<u>341,902</u>	<u>346,789</u>
DEDUCT:			
CURRENT LIABILITIES			
Bank and other borrowings	<i>24</i>	191,417	196,394
Notes payable	<i>25</i>	124,937	103,695
Trade payables	<i>26</i>	82,090	66,202
Other payables and accruals		67,034	57,783
Deferred income	<i>17</i>	973	–
Amounts due to directors	<i>27</i>	4,222	1,586
Tax payable		1,977	1,631
		<u>472,650</u>	<u>427,291</u>
NET CURRENT LIABILITIES		<u>(130,748)</u>	<u>(80,502)</u>
		<u>111,490</u>	<u>162,878</u>

Consolidated Balance Sheet (continued)

As at July 2004

	<i>Notes</i>	2004 HK\$'000	2003 HK\$'000 (Restated)
REPRESENTING:			
SHARE CAPITAL	28	25,000	25,000
RESERVES	30	50,945	94,736
SHAREHOLDERS' FUNDS		75,945	119,736
MINORITY INTERESTS		11,036	16,034
NON-CURRENT LIABILITIES			
Bank and other borrowings	24	20,649	26,741
Deferred income	17	3,540	–
Deferred tax liability	10(b)	320	367
		24,509	27,108
		111,490	162,878

APPROVED AND AUTHORISED FOR ISSUE BY
THE BOARD OF DIRECTORS ON 25 OCTOBER 2004

Wong Sai Wa
Director

Kwan Kai Cheong
Director

Balance Sheet

As at 31 July 2004

	<i>Notes</i>	2004 HK\$'000	2003 HK\$'000
NON-CURRENT ASSETS			
Fixed assets	13	6	9
Interests in subsidiaries	16	66,075	66,145
		66,081	66,154
CURRENT ASSETS			
Deposits, prepayments and other receivables	22	44	12,741
Pledged deposits	23	–	5,000
Cash and cash equivalents	23	41,386	36,650
		41,430	54,391
DEDUCT:			
CURRENT LIABILITIES			
Bank and other borrowings	24	26,741	10,000
Other payables and accruals		5,660	5,837
Amount due to a director	27	642	–
		33,043	15,837
NET CURRENT ASSETS			
		8,387	38,554
		74,468	104,708
REPRESENTING:			
SHARE CAPITAL			
	28	25,000	25,000
RESERVES			
	30	49,468	52,967
SHAREHOLDERS' FUNDS			
		74,468	77,967
NON-CURRENT LIABILITY			
Bank and other borrowings	24	–	26,741
		74,468	104,708

APPROVED AND AUTHORISED FOR ISSUE BY
THE BOARD OF DIRECTORS ON 25 OCTOBER 2004

Wong Sai Wa
Director

Kwan Kai Cheong
Director

Consolidated Cash Flow Statement

For the Year ended 31 July 2004

	Notes	2004 HK\$'000	2003 HK\$'000
CASH FLOWS FROM OPERATING ACTIVITIES			
Loss before tax		(43,471)	(1,465)
Adjustments for:			
Finance costs		14,555	9,415
Share of results of an associate		(1,449)	1,202
Gain on disposal of a subsidiary		(1,641)	–
Interest income		(1,197)	(1,553)
Depreciation		16,261	9,007
Amortisation of deferred income		(568)	–
Loss on disposal of fixed assets		18	67
Provision for bad and doubtful debts		20,204	2,159
Amortisation of intangible assets		3,981	3,858
Amortisation of goodwill		1,048	477
Negative goodwill recognised		(694)	(695)
		<u>7,047</u>	<u>22,472</u>
Operating profit before working capital changes		7,047	22,472
Decrease in inventories		8,130	6,182
(Increase)/decrease in trade receivables		(11,083)	7,037
(Increase)/decrease in deposits, prepayments and other receivables		(12,136)	34,934
Increase/(decrease) in trade payables		15,888	(9,929)
Increase/(decrease) in notes payable		21,242	(7,960)
Increase/(decrease) in other payables and accruals		3,241	(14,859)
Increase/(decrease) in amounts due to directors		2,636	(6,544)
		<u>34,965</u>	<u>31,333</u>
Cash generated from operations		34,965	31,333
Interest received		2,232	758
Interest paid on bank and other borrowings		(13,499)	(8,579)
		<u>23,698</u>	<u>23,512</u>
NET CASH FROM OPERATING ACTIVITIES		23,698	23,512
CASH FLOWS FROM INVESTING ACTIVITIES			
Purchases of fixed assets		(7,286)	(25,515)
Proceeds from disposal of fixed assets		181	3
Decrease in long term prepayments		5,405	6,181
Acquisition of a subsidiary	31(a)	(7,624)	13,348
Disposal of a subsidiary	31(b)	(9)	–
Repayment from an associate		–	291
Increase in pledged deposits		(2,137)	(12,325)
		<u>(11,470)</u>	<u>(18,017)</u>
NET CASH USED IN INVESTING ACTIVITIES		(11,470)	(18,017)

Consolidated Cash Flow Statement *(continued)*

For the Year ended 31 July 2004

	2004 HK\$'000	2003 HK\$'000
CASH FLOWS FROM FINANCING ACTIVITIES		
New bank loans	136,610	84,309
Repayment of bank loans	(147,080)	(79,606)
Repayment of other loans	(599)	(199)
(Repayment to)/advances from minority shareholders	(3,344)	3,968
Capital injection by minority shareholders	–	400
	<u> </u>	<u> </u>
NET CASH (USED IN)/FROM FINANCING ACTIVITIES	<u>(14,413)</u>	<u>8,872</u>
NET (DECREASE)/INCREASE IN CASH AND CASH EQUIVALENTS	(2,185)	14,367
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	<u>45,754</u>	<u>31,387</u>
CASH AND CASH EQUIVALENTS AT END OF YEAR	<u>43,569</u>	<u>45,754</u>
ANALYSIS OF THE BALANCES OF CASH AND CASH EQUIVALENTS		
Non-pledged cash and bank balances	2,195	9,449
Non-pledged time deposits with original maturity of less than three months when acquired	41,374	36,305
	<u> </u>	<u> </u>
	<u>43,569</u>	<u>45,754</u>

Consolidated Statement of Changes in Equity

For the Year ended 31 July 2004

	Share capital HK\$'000	Share premium HK\$'000	Capital reserve HK\$'000	Exchange fluctuation reserve HK\$'000	Retained profits HK\$'000	Total HK\$'000
At 1 August 2002	25,000	17,992	27,104	25	50,267	120,388
Loss for the year	—	—	—	—	(652)	(652)
At 31 July 2003 and 1 August 2003	25,000	17,992	27,104	25	49,615	119,736
Loss for the year	—	—	—	—	(43,791)	(43,791)
At 31 July 2004	25,000	17,992	27,104	25	5,824	75,945
Reserves retained by:						
Company and subsidiaries	25,000	17,992	27,104	25	5,849	75,970
An associate	—	—	—	—	(25)	(25)
At 31 July 2004	25,000	17,992	27,104	25	5,824	75,945
Company and subsidiaries	25,000	17,992	27,104	25	51,089	121,210
An associate	—	—	—	—	(1,474)	(1,474)
At 31 July 2003	25,000	17,992	27,104	25	49,615	119,736

Notes to Financial Statements

For the Year ended 31 July 2004

1. CORPORATE INFORMATION

The registered office of China Medical Science Limited is located at Ugland House, P.O. Box 309, George Town, Grand Cayman, Cayman Islands, British West Indies.

The Group is involved in the development, production, sale and distribution of packaging materials for biotechnological and pharmaceutical products, and a range of biotechnological and pharmaceutical products for human use as well as for cattle and other domestic animals, such as pigs, sheep and poultry, in the People's Republic of China (the "PRC").

In the opinion of the directors, the ultimate holding company of the Company is Concord Business Management Limited, a company incorporated in the British Virgin Islands.

2. BASIS OF PRESENTATION

As at 31 July 2004, the Group had net current liabilities of approximately HK\$130,748,000. Bank indebtedness comprising short term bank loans and notes payable of HK\$155,308,000 and HK\$124,937,000 respectively represented a majority of the total current liabilities.

The short term bank loans and the banking facilities relating to notes payable have been renewed in the past by the banks on their maturity dates and it is the opinion of the directors that such short term bank loans and banking facilities will continue to be renewed upon maturity after the balance sheet date. Accordingly, the directors are satisfied that it is appropriate to prepare the financial statements on a going concern basis, notwithstanding the Group's net current liabilities position as at 31 July 2004.

3. PRINCIPAL ACCOUNTING POLICIES

(a) Basis of preparation

These financial statements have been prepared in accordance with accounting principles generally accepted in Hong Kong and comply with Statements of Standard Accounting Practice ("SSAPs") issued by the Hong Kong Institute of Certified Public Accountants (the "HKICPA") and are prepared under the historical cost convention.

In the current year, the Group adopted SSAP 12 (revised) "Income taxes" issued by the HKICPA which is effective for the current year's financial statements.

Notes to Financial Statements

For the Year ended 31 July 2004

3. PRINCIPAL ACCOUNTING POLICIES (continued)

(a) Basis of preparation (continued)

The principal effect of the implementation of SSAP 12 (revised) is in relation to deferred tax. In previous years, partial provision was made for deferred tax using the income statement liability method, i.e. a liability was recognised in respect of timing differences arising, except where those timing differences were not expected to reverse in the foreseeable future. SSAP 12 (revised) requires the adoption of a balance sheet liability method, whereby deferred tax is recognised in respect of all temporary differences between the carrying amounts of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable profits, with limited exception.

The change in accounting policy has been accounted for retrospectively. Comparative amount for 2003 have been restated accordingly. This has resulted in increases in the opening balances of goodwill and deferred tax liability as at 1 August 2003 of approximately HK\$367,000 each. The Group's loss for 2004 was decreased by approximately HK\$9,000.

(b) Basis of consolidation

The consolidated financial statements include the financial statements of the Company and its subsidiaries for the year ended 31 July 2004. The results of subsidiaries acquired or disposed of during the year are consolidated from or to their effective dates of acquisition or disposal, respectively. All significant inter-company transactions and balances within the Group are eliminated on consolidation.

Minority interests represent the interests of outside shareholders in results and net assets of the Company's subsidiaries.

(c) Revenue recognition

Revenue from sale of goods is recognised when the significant risks and rewards of ownership have been transferred to the buyer.

Interest income is recognised on a time proportion basis, taking into account the principal amounts outstanding and the interest rates applicable.

(d) Fixed assets and depreciation

Fixed assets, other than construction in progress, are stated at cost less aggregate depreciation and impairment losses. The cost of an asset comprises its purchase price and any directly attributable costs of bringing the asset to its working condition and location for its intended use. Expenditure incurred after the fixed assets have been put into operation, such as repairs and maintenance, is normally charged to the income statement in the period in which it is incurred. In situations where it can be clearly demonstrated that the expenditure has resulted in an increase in the future economic benefits expected to be obtained from the use of the fixed asset, the expenditure is capitalised as an additional cost of that asset.

Notes to Financial Statements

For the Year ended 31 July 2004

3. PRINCIPAL ACCOUNTING POLICIES (continued)

(d) Fixed assets and depreciation (continued)

Other than construction in progress, depreciation is calculated to write off the cost of other assets over their estimated useful life using the straight line basis at the following annual rates:

Leasehold land and buildings	Over the terms of the joint venture or land use right, whichever is shorter
Plant and machinery	10%
Furniture, fixtures and office equipment	20%
Motor vehicles	20%
Computer equipment	20%

The gain or loss on disposal of the fixed assets representing the difference between the net sales proceeds and the carrying amounts of the relevant assets is recognised in the income statement.

Construction in progress is stated at cost less any impairment losses, and is not depreciated. Cost comprises direct costs of construction and capitalised borrowing costs on related borrowed funds during the period of construction. Construction in progress is reclassified to the appropriate category of fixed assets when completed and ready for use.

(e) Subsidiaries

A subsidiary is an enterprise over which the Company has control either directly or indirectly. Control is the power to govern the financial and operating policies of a company so as to obtain benefits from its activities.

Investments in subsidiaries are stated in the Company's balance sheet at cost less any impairment losses. Income from subsidiaries is recognised in the Company's financial statements on the basis of dividends declared by the subsidiaries.

Notes to Financial Statements

For the Year ended 31 July 2004

3. PRINCIPAL ACCOUNTING POLICIES *(continued)*

(f) Jointly-controlled operations

A jointly-controlled operation is a joint operation, which is subject to joint control, resulting in none of the participating parties having unilateral control over the economic activity of the jointly-controlled operation.

A joint venture arrangement which involves the use of the assets and other reserves of the Group and other parties, without establishment of a separate entity, is referred to as jointly-controlled operations. Under this arrangement, assets remain under the ownership and control of each party. Revenue and expenses incurred in common are shared by the parties according to the contractual arrangement.

Assets that the Group controls and liabilities that it incurs in relation to jointly-controlled operations are recognised in the Group's consolidated balance sheet on an accrual basis and are classified according to the nature of the item. The Group's share of the income that it earns from jointly-controlled operations, together with the expenses that it incurs, are included in the Group's consolidated income statement.

(g) Associates

An associate is a company, not being a subsidiary or a jointly-controlled entity, in which the Group has a long term interest of generally not less than 20% of the equity voting rights and over which it is in a position to exercise significant influence.

The Group's share of the post-acquisition results and reserves of associates is included in the consolidated income statement and consolidated reserves, respectively. The Group's interests in associates are stated in the consolidated balance sheet at the Group's share of net assets under the equity method of accounting, less any impairment losses.

(h) Goodwill

Goodwill arising on the acquisition of subsidiaries and associates represents the excess of the cost of the acquisition over the Group's share of the fair values of the identifiable assets and liabilities acquired as at the date of acquisition.

Goodwill arising on acquisition is recognised in the consolidated balance sheet as an asset and amortised on the straight line basis over its estimated useful life of 20 years. In the case of associates, any unamortised goodwill is included in the carrying amount thereof, rather than as a separately identified asset on the consolidated balance sheet.

Notes to Financial Statements

For the Year ended 31 July 2004

3. PRINCIPAL ACCOUNTING POLICIES (continued)

(h) Goodwill (continued)

On disposal of subsidiaries and associates, the gain or loss on disposal is calculated by reference to the net assets at the date of disposal, including the attributable amount of goodwill which remains unamortised and any relevant reserves, as appropriate.

The carrying amount of goodwill is reviewed annually and written down for impairment when it is considered necessary. A previously recognised impairment loss for goodwill is not reversed unless the impairment loss was caused by a specific external event of an exceptional nature that was not expected to recur, and subsequent external events have occurred which have reversed the effect of that event.

(i) Negative goodwill

Negative goodwill arising on the acquisition of subsidiaries and associates represents the excess of the Group's share of the fair values of the identifiable assets and liabilities acquired as at the date of acquisition, over the cost of the acquisition.

To the extent that negative goodwill relates to expectations of future losses and expenses that are identified in the acquisition plan and that can be measured reliably, but which do not represent identifiable liabilities as at the date of acquisition, that portion of negative goodwill is recognised as income in the consolidated income statement when the future losses and expenses are recognised.

To the extent that negative goodwill does not relate to identifiable expected future losses and expenses as at the date of acquisition, negative goodwill is recognised in the consolidated income statement on a systematic basis over the remaining average useful life of the acquired depreciable/amortisable assets. The amount of any negative goodwill in excess of the fair values of the acquired non-monetary assets is recognised as income immediately.

In the case of associates, any negative goodwill not yet recognised in the consolidated income statement is included in the carrying amount thereof, rather than as a separately identified item on the consolidated balance sheet.

On disposal of subsidiaries and associates, the gain or loss on disposal is calculated by reference to the net assets at the date of disposal, including the attributable amount of negative goodwill which has not been recognised in the consolidated income statement and any relevant reserves as appropriate.

Notes to Financial Statements

For the Year ended 31 July 2004

3. PRINCIPAL ACCOUNTING POLICIES (continued)

(j) Intangible assets

Purchased patents and licences are stated at cost less aggregate amortisation and any impairment losses, and are amortised on a straight line basis over the following years of estimated useful lives:

Technical know-how	Over the terms of the joint venture or 7 years, whichever is shorter
Production licences	Over the terms of the joint venture or 5 years, whichever is shorter

(k) Research and development costs

All research costs are charged to the income statement as incurred.

Expenditure incurred on projects to develop new products is capitalised and deferred only when the projects are clearly defined; the expenditure is separately identifiable and can be measured reliably; there is reasonable certainty that the projects are technically feasible; and the products have commercial value. Product development expenditure which does not meet these criteria is expensed when incurred.

(l) Long term investments

Long term investments are non-trading investments in unlisted equity securities intended to be held on a long term basis and are stated at cost less provision for impairment in value, other than those considered to be temporary in nature, which are considered necessary by the directors, on an individual basis.

(m) Inventories

Inventories are stated at the lower of cost and net realisable value. Cost is determined on the weighted average basis and, in the case of work in progress and finished goods, comprises direct materials, direct labour and an appropriate proportion of overheads. Net realisable value is based on estimated selling prices less any estimated costs to be incurred to completion and disposal.

(n) Impairment of assets

The carrying amounts of the Group's assets are reviewed at each balance sheet date to determine whether there is any indication of impairment. If any such indication exists, the asset's recoverable amount is estimated. An impairment loss is recognised whenever the carrying amount of an asset or its cash-generating unit exceeds its recoverable amount. Impairment losses are recognised in the income statement.

Notes to Financial Statements

For the Year ended 31 July 2004

3. PRINCIPAL ACCOUNTING POLICIES (continued)

(o) Provisions

A provision is recognised in the balance sheet when the Group has a legal or constructive obligation as a result of a past event and it is probable that a future outflow of economic benefits will be required to settle the obligation. If the effect is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability.

(p) Convertible notes

Convertible notes are separately disclosed and regarded as liabilities unless conversion actually occurs. The associated finance cost is recognised in the income statement on an accrual basis while the associated costs of issue are charged immediately to the income statement when it is incurred.

(q) Leases

Rentals payable under operating leases are charged to the income statement on a straight line basis over the terms of the relevant leases.

(r) Foreign currency translation

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 market exchange rates ruling at the balance sheet date. Differences on foreign currency translation are dealt with in the income statement.

The consolidated financial statements are prepared by using the net investment method such that the balance sheets of the Company's overseas subsidiaries are translated in Hong Kong dollars at the market exchange rate ruling at the balance sheet date, while their income statements are translated at the average exchange rate for the year. Any exchange differences arising on such translation are dealt with in the exchange fluctuation reserve.

(s) Employee benefits

Salaries, annual bonuses, annual leave entitlements 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.

Notes to Financial Statements

For the Year ended 31 July 2004

3. PRINCIPAL ACCOUNTING POLICIES (continued)

(s) Employee benefits (continued)

Obligations for contributions to retirement plans, including contributions payable under the Hong Kong Mandatory Provident Fund Schemes Ordinance and the PRC central pension scheme, are recognised as an expense in the income statement as incurred.

Termination benefits are recognised when, and only when, the Group demonstrably commits itself to terminate employment or to provide benefits as a result of voluntary redundancy by having a detailed formal plan which is without realistic possibility of withdrawal.

When the Group grants employees options to acquire shares of the Company for nil consideration, no employee benefit cost or obligation is recognised at the date of grant. When the options are exercised, equity is increased by the amount of the proceeds received.

(t) Income tax

Income tax expense represents the sum of the tax currently payable and deferred tax.

The tax currently payable is based on taxable profit for the year. Taxable profit differs from net profit as reported in the income statement because it excludes items of income and expense that are taxable or deductible in other years, and it further excludes income statement items that are never taxable and deductible.

Deferred tax is the tax expected to be payable or recoverable on differences between the carrying amounts of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable profit, and is accounted for using the balance sheet liability method. Deferred tax liabilities are generally recognised for all taxable temporary differences, and deferred tax assets are recognised to the extent that it is probable that taxable profits will be available against which deductible temporary differences can be utilised. Such assets and liabilities are not recognised if the temporary difference arises from goodwill (or negative goodwill) or from the initial recognition (other than in a business combination) of other assets and liabilities in a transaction that affects neither the taxable profit nor the accounting profit.

The carrying amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered.

Deferred tax is calculated at the tax rates that are expected to apply in the period when the liability is settled or the asset is realised. Deferred tax is charged or credited in the income statement, except when it relates to items charged or credited directly to equity, in which case the deferred tax is also dealt with in equity.

Notes to Financial Statements

For the Year ended 31 July 2004

3. PRINCIPAL ACCOUNTING POLICIES *(continued)*

(u) Related parties

Parties are considered to be related if one party has the ability, directly or indirectly, to control the other party or exercise significant influence over the other party in making financial and operating decisions. Parties are also considered to be related if they are subject to common control or common significant influence.

(v) 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.

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. Segment revenue, expenses, assets and liabilities are determined before intra-group balances 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.

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

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

(w) Cash equivalents

Cash equivalents are short-term, highly liquid investments which are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value.

Notes to Financial Statements

For the Year ended 31 July 2004

4. SEGMENT INFORMATION

Segment information is presented by way of two segment formats: (i) on a primary segment reporting basis, by business segment; and (ii) on a secondary segment reporting basis, by geographical segment.

The Group's operating businesses are structured and managed separately, according to the nature of their operations and the products and services they provide. Each of the Group's business segments represents a strategic business unit that offers products and services which are subject to risks and returns that are different from those of the other business segments. Summary details of the business segments are as follows:

- (a) the human drugs segment comprises the production, sales and distribution of infusion and non-infusion medicine;
- (b) the veterinary drugs segment comprises the production, sales and distribution of veterinary drugs;
- (c) the packaging materials segment comprises the production, sales and distribution of packaging materials for infusion medicine; and
- (d) the corporate segment comprises corporate income and expense items.

During the year, the entire turnover and contribution to (loss)/profit from operating activities of the Group were derived from the principal activities carried out in the PRC. Accordingly, a further analysis by geographical segment is not presented.

Inter-segment sales and transfers are transacted with reference to the selling prices used for sales made to third parties at the then prevailing market prices.

Notes to Financial Statements

For the Year ended 31 July 2004

4. SEGMENT INFORMATION (continued)

Business segments

The following tables present revenue, (loss)/profit and certain asset, liability and expenditure information for the Group's business segments.

	Human drugs		Veterinary drugs		Packaging materials		Corporate		Eliminations		Consolidated	
	2004	2003	2004	2003	2004	2003	2004	2003	2004	2003	2004	2003
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Segment revenue:												
Sales to external customers	129,056	68,186	24,953	23,025	17,524	36,835	-	-	-	-	171,533	128,046
Inter-segment sales	13,416	2,995	-	-	667	944	-	-	(14,083)	(3,939)	-	-
Other revenue	2,864	20	73	-	3	-	1,826	2,391	(1,130)	(1,696)	3,636	715
Total revenue	145,336	71,201	25,026	23,025	18,194	37,779	1,826	2,391	(15,213)	(5,635)	175,169	128,761
Segment results	(15,472)	6,255	1,169	4,669	(13,204)	373	(4,055)	(3,698)	-	-	(31,562)	7,599
Interest income											1,197	1,553

Notes to Financial Statements

For the Year ended 31 July 2004

4. SEGMENT INFORMATION (continued)

Business segments (continued)

	Human drugs		Veterinary drugs		Packaging materials		Corporate		Eliminations		Consolidated	
	2004	2003	2004	2003	2004	2003	2004	2003	2004	2003	2004	2003
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
(Loss)/profit from operating activities												
Finance costs											(30,365)	9,152
Share of results of an associate	1,449	(1,202)	-	-	-	-	-	-	-	-	1,449	(1,202)
Loss before tax											(43,471)	(1,465)
Tax expense	17	-	(354)	(556)	-	(227)	-	-	-	-	(337)	(783)
Loss before minority interests											(43,808)	(2,248)
Minority interests											17	1,596
Loss attributable to shareholders											(43,791)	(652)

Notes to Financial Statements

For the Year ended 31 July 2004

4. SEGMENT INFORMATION (continued)

Business segments (continued)

	Human drugs		Veterinary drugs		Packaging materials		Corporate		Eliminations		Consolidated	
	2004	2003	2004	2003	2004	2003	2004	2003	2004	2003	2004	2003
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Segment assets	354,051	334,923	104,463	93,660	99,310	116,109	151,123	132,540	(134,390)	(95,197)	574,557	582,035
Interest in an associate	9,583	8,134	-	-	-	-	-	-	-	-	9,583	8,134
Total assets	363,634	343,057	104,463	93,660	99,310	116,109	151,123	132,540	(134,390)	(95,197)	584,140	590,169
Segment liabilities	377,271	326,974	71,676	50,566	90,696	70,913	91,906	101,143	(134,390)	(95,197)	497,159	454,399
Total liabilities	377,271	326,974	71,676	50,566	90,696	70,913	91,906	101,143	(134,390)	(95,197)	497,159	454,399
Other segment information:												
Depreciation and amortisation (excluding goodwill and negative goodwill)	14,189	7,504	3,096	2,775	2,939	2,571	18	15	-	-	20,242	12,865
Amortisation of goodwill	-	-	-	-	-	-	1,048	477	-	-	1,048	477
Recognition of negative goodwill	-	-	-	-	-	-	(694)	(695)	-	-	(694)	(695)
Amortisation of deferred income	(568)	-	-	-	-	-	-	-	-	-	(568)	-
Capital expenditure	9,133	9,359	3,051	3,711	183	12,417	-	28	-	-	12,367	25,515

Notes to Financial Statements

For the Year ended 31 July 2004

5. TURNOVER, OTHER REVENUE AND GAINS

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

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

	2004 HK\$'000	2003 HK\$'000
Turnover		
Sale of human drugs	129,056	68,186
Sale of veterinary drugs	24,953	23,025
Sale of packaging materials	17,524	36,835
	<u>171,533</u>	<u>128,046</u>
	-----	-----
Other revenue and gains		
Interest income	1,197	1,553
Sundry income	733	20
Negative goodwill recognised	694	695
Amortisation of deferred income (note 17)	568	-
Gain on disposal of a subsidiary	1,641	-
	<u>4,833</u>	<u>2,268</u>
	-----	-----
	<u>176,366</u>	<u>130,314</u>
	-----	-----

Notes to Financial Statements

For the Year ended 31 July 2004

6. (LOSS)/PROFIT FROM OPERATING ACTIVITIES

(Loss)/profit from operating activities is arrived at after charging/(crediting):

	2004 HK\$'000	2003 HK\$'000
Amortisation of goodwill	1,048	477
Amortisation of intangible assets	3,981	3,858
Auditors' remuneration	320	450
Cost of inventories sold	137,446	92,102
Depreciation	16,261	9,007
Guaranteed return (note 17)	1,483	–
Sales proceeds	(181)	(3)
Less: Net book value	199	70
Loss on disposal of fixed assets	18	67
Minimum operating lease payments for land and buildings	715	682
Research and development expenditure	1,516	977
Staff cost (including directors' emoluments in note 8):		
Salaries, wages and other allowances	7,969	8,036
Pension scheme contributions	343	460
	8,312	8,496

7. FINANCE COSTS

	2004 HK\$'000	2003 HK\$'000
Interest on bank loans wholly repayable within five years	13,386	7,838
Interest on other loans	634	775
Interest on convertible note	535	802
	14,555	9,415

Notes to Financial Statements

For the Year ended 31 July 2004

8. DIRECTORS' AND EMPLOYEES' EMOLUMENTS

	2004 HK\$'000	2003 HK\$'000
(a) Directors		
Fees		
Executive directors	360	360
Independent non-executive directors	240	270
	<u>600</u>	<u>630</u>
Other emoluments for executive directors		
Salaries, allowances and benefits in kind	68	68
	<u>668</u>	<u>698</u>

The remuneration paid by the Group to two (2003: two) executive directors of the Company for the year ended 31 July 2004 analysed on an individual basis was approximately HK\$360,000 (2003: HK\$360,000) and HK\$68,000 (2003: HK\$68,000) respectively. The remuneration paid by the Group to the two (2003: four) independent non-executive directors of the Company for the year ended 31 July 2004 was HK\$120,000 each (2003: HK\$10,000, HK\$70,000, HK\$70,000 and HK\$120,000 respectively). The remaining three (2003: four) directors did not receive any remuneration during the year.

There was no arrangement under which a director waived or agreed to waive any remuneration during the year.

Notes to Financial Statements

For the Year ended 31 July 2004

8. DIRECTORS' AND EMPLOYEES' EMOLUMENTS (continued)

(b) Five highest paid employees

The five highest paid employees during the year included three (2003: three) directors, details of whose remuneration are set out in note 8(a) above. Details of the remuneration of the remaining two (2003: two) highest paid non-director employees are as follows:

	2004 HK\$'000	2003 HK\$'000
Salaries and allowances	518	420
Pension scheme contributions	<u>12</u>	<u>12</u>
	<u>530</u>	<u>432</u>

The number of highest paid non-director employees whose remuneration fell within the following band were:

	2004	2003
Nil – HK\$1,000,000	<u>2</u>	<u>2</u>

During the year, no emoluments were paid by the Group to the directors or the other highest paid employees either as an inducement to join the Group, or as compensation for loss of office (2003: Nil).

9. PENSION SCHEME

The Group operates a defined contribution Mandatory Provident Fund retirement benefits scheme (the "MPF Scheme") under the Mandatory Provident Fund Schemes Ordinance, for all of those employees who are eligible to participate in the scheme. Contributions are made based on a percentage of the employees' basic salaries and are charged to the income statement as they become payable in accordance with the rules of the MPF Scheme. The assets of the MPF Scheme are held separately from those of the Group in an independently administered fund. The Group's employer contributions vest fully with the employees when contributed into the MPF Scheme.

Notes to Financial Statements

For the Year ended 31 July 2004

9. PENSION SCHEME (continued)

The employees of the Company's subsidiaries which operate in the PRC are required to participate in a central pension scheme operated by the local municipal government. The PRC subsidiaries are required to contribute a percentage of its payroll costs to the central pension scheme. The central pension scheme is responsible for the entire pension obligations payable to all retired employees and the Group has no further obligations for the pension payments on post-retirement benefits beyond the annual contributions.

During the year, the Group made pension contributions of HK\$343,000 (2003: HK\$460,000).

10. TAX

(a) Tax expense in the consolidated income statement represents:

	2004 HK\$'000	2003 HK\$'000
Current tax:		
PRC	346	783
Deferred tax (note 10(b)):		
Current year	(9)	–
Tax expense	<u>337</u>	<u>783</u>

No provision for Hong Kong profits tax has been made as the Group had no estimated assessable profits arising in Hong Kong for both years. Current tax represents PRC enterprise income tax charge on the estimated taxable profits of certain subsidiaries operating in the PRC calculated at the prevailing tax rate.

Tax expense for the year can be reconciled as follows:

	2004 HK\$'000	2003 HK\$'000
Loss before tax	<u>(43,471)</u>	<u>(1,465)</u>
Tax effect at the PRC statutory income tax rate of 33%	(14,345)	(483)
Tax effect of non-deductible expenses/tax exempt revenue	431	(555)
Tax effect of unrecognised general provision for bad and doubtful debts	6,667	712
Tax effect of unrecognised tax losses	<u>7,584</u>	<u>1,109</u>
Tax expense	<u>337</u>	<u>783</u>

Notes to Financial Statements

For the Year ended 31 July 2004

10. TAX (continued)

(b) Deferred tax (asset)/liability in the consolidated balance sheet represent:

	Decelerated depreciation allowances	Accelerated depreciation allowances	Total
	HK\$'000	HK\$'000	HK\$'000
Acquisition of subsidiaries (note 31(a)) and at 31.7.2003 and 1.8.2003	–	367	367
Acquisition of a subsidiary (note 31(a))	(265)	–	(265)
Disposal of a subsidiary (note 31(b))	–	(30)	(30)
Charge/(credit) for the year	8	(17)	(9)
	<u> </u>	<u> </u>	<u> </u>
At 31.7.2004	(257)	320	63
	<u> </u>	<u> </u>	<u> </u>

(c) The components of unrecognised deductible temporary differences are as follows:

	2004	2003
	HK\$'000	HK\$'000
Unutilised tax losses	26,343	3,361
General provision for bad and doubtful debts	39,376	19,172
	<u> </u>	<u> </u>
	65,719	22,533
	<u> </u>	<u> </u>

Deductible temporary differences have not been recognised in these financial statements owing to the absence of objective evidence in respect of the availability of sufficient taxable profits that are expected to arise to offset against the deductible temporary differences.

The unutilised tax losses accumulated in the PRC subsidiaries would expire in five years from the respective year of loss.

(d) At the balance sheet date, the Company had no taxable or deductible temporary differences.

11. LOSS ATTRIBUTABLE TO SHAREHOLDERS

Loss attributable to shareholders includes a loss of HK\$3,499,000 (2003: HK\$2,972,000) which has been dealt with in the financial statements of the Company.

Notes to Financial Statements

For the Year ended 31 July 2004

12. LOSS PER SHARE

The calculation of basic loss per share is based on the loss attributable to shareholders for the year of HK\$43,791,000 (2003: HK\$652,000) and the weighted average number of 500,000,000 (2003: 500,000,000) ordinary shares in issue during the year.

The diluted loss per share has not been disclosed as the convertible note outstanding during the year and the potential ordinary shares issuable under the Company's share option schemes have no dilutive effect.

13. FIXED ASSETS

(a) The Group

	Leasehold land and buildings HK\$'000	Plant and machinery HK\$'000	Furniture, fixtures and office equipment HK\$'000	Motor vehicles HK\$'000	Computer equipment HK\$'000	Construction in progress HK\$'000	Total HK\$'000
Cost:							
At 1 August 2003	150,568	63,826	904	5,163	1,552	8,301	230,314
Additions	808	4,633	96	359	71	6,400	12,367
Acquisition of a subsidiary (note 31(a))	-	321	-	321	14	-	656
Disposals	(226)	(107)	-	(128)	-	-	(461)
Reclassification	1,959	3,900	-	-	-	(5,859)	-
At 31 July 2004	153,109	72,573	1,000	5,715	1,637	8,842	242,876
Aggregate depreciation:							
At 1 August 2003	9,810	12,822	329	2,350	664	-	25,975
Charge for the year	4,323	10,069	429	1,281	159	-	16,261
Written back on disposals	(63)	(77)	-	(122)	-	-	(262)
At 31 July 2004	14,070	22,814	758	3,509	823	-	41,974
Net book value:							
At 31 July 2004	139,039	49,759	242	2,206	814	8,842	200,902
At 31 July 2003	140,758	51,004	575	2,813	888	8,301	204,339

Notes to Financial Statements

For the Year ended 31 July 2004

13. FIXED ASSETS (continued)

(a) The Group (continued)

All the Group's leasehold land and buildings are situated in the PRC. As at 31 July 2004, the cost of the leasehold land and buildings held under long term and medium term leases were HK\$18,991,000 (2003: HK\$18,991,000) and HK\$134,118,000 (2003: HK\$131,577,000) respectively.

As at 31 July 2004, the relevant title certificate for a piece of land with cost of approximately HK\$146,000 (2003: HK\$146,000) and net book value of approximately HK\$126,000 (2003: HK\$131,000) is in the process of being transferred to one of the Company's subsidiaries.

As at 31 July 2004, certain of the Group's leasehold land and buildings and plant and machinery with net book values of approximately HK\$64,413,000 (2003: HK\$68,337,000) and HK\$29,290,000 (2003: HK\$35,232,000) respectively were pledged to secure general banking facilities granted to the Group (note 24).

(b) The Company

	Computer equipment HK\$'000
Cost:	
At 1 August 2003 and at 31 July 2004	15
Aggregate depreciation:	
At 1 August 2003	6
Charge for the year	3
At 31 July 2004	9
Net book value:	
At 31 July 2004	6
At 31 July 2003	9

Notes to Financial Statements

For the Year ended 31 July 2004

14. INTANGIBLE ASSETS

	Technical know-how HK\$'000	Production licenses HK\$'000	Total HK\$'000
Cost:			
At 1 August 2003	11,642	10,060	21,702
Acquisition of a subsidiary (note 31(a))	—	6,924	6,924
	<u>11,642</u>	<u>16,984</u>	<u>28,626</u>
At 31 July 2004	11,642	16,984	28,626
Aggregate amortisation:			
At 1 August 2003	5,266	6,951	12,217
Charge for the year	1,663	2,318	3,981
	<u>6,929</u>	<u>9,269</u>	<u>16,198</u>
At 31 July 2004	6,929	9,269	16,198
Net book value:			
At 31 July 2004	4,713	7,715	12,428
At 31 July 2003	<u>6,376</u>	<u>3,109</u>	<u>9,485</u>

Notes to Financial Statements

For the Year ended 31 July 2004

15. GOODWILL AND NEGATIVE GOODWILL

	Goodwill HK\$'000	Negative goodwill HK\$'000
Cost:		
At 1 August 2003		
As previously reported	18,670	(8,333)
Prior period adjustment in respect of deferred tax	367	–
As restated	19,037	(8,333)
Acquisition of a subsidiary (note 31(a))	3,593	–
Disposal of a subsidiary (note 31(b))	(190)	–
	<u>22,440</u>	<u>(8,333)</u>
At 31 July 2004	22,440	(8,333)
Aggregate amortisation/(recognition as income):		
At 1 August 2003	1,306	(2,199)
Amortisation/(recognised as income) for the year	1,048	(694)
Written back on disposal of a subsidiary (note 31(b))	(2)	–
	<u>2,352</u>	<u>(2,893)</u>
At 31 July 2004	2,352	(2,893)
Net book value:		
At 31 July 2004	20,088	(5,440)
At 31 July 2003	17,731	(6,134)

16. INTERESTS IN SUBSIDIARIES

	2004 HK\$'000	2003 HK\$'000
Unlisted shares, at cost	42,876	42,876
Amounts due from subsidiaries	26,751	26,806
Amount due to a subsidiary	(3,552)	(3,537)
	<u>66,075</u>	<u>66,145</u>

The amounts with subsidiaries are interest-free, unsecured and have no fixed terms of repayment.

Notes to Financial Statements

For the Year ended 31 July 2004

16. INTERESTS IN SUBSIDIARIES (continued)

Particulars of the subsidiaries as at 31 July 2004 are as follows:

Name	Place of incorporation/ establishment and operations	Nominal value of issued ordinary share/registered share capital	Percentage of equity attributable to the Company		Principal activities
			Directly	Indirectly	
China Biotechnology Limited	Cayman Islands	US\$3	100.00	–	Investment holding
Glazier Limited	British Virgin Islands	US\$2	–	100.00	Investment holding
Seechain Investments Limited	British Virgin Islands	US\$1	–	100.00	Investment holding
Sichuan Future Industrial Co., Ltd.*	PRC	RMB23,980,000	–	91.00	Manufacture and distribution of medical caps
Chengdu Viking Yuan Heng Pharmaceutical Co., Ltd.*	PRC	RMB18,000,000	–	91.00	Manufacture and distribution of veterinary drugs
Chengdu Mt. Green Pharmaceutical Co., Ltd.*	PRC	RMB18,000,000	–	91.00	Manufacture and sale of infusion medicine
Sichuan Shule Pharmaceutical Joint Stock Co., Ltd.**	PRC	RMB18,000,000	–	46.46	Manufacture and sale of human drugs
樂山裕恆藥業有限公司*	PRC	RMB7,000,000	–	34.61	Manufacture and sale of human drugs
四川利亨生物藥業有限公司#	PRC	RMB3,096,800	–	72.80	Manufacture and distribution of veterinary drugs

* Sino-foreign joint venture enterprise

** Joint-stock enterprise

Acquired during the year

Notes to Financial Statements

For the Year ended 31 July 2004

17. INTEREST IN A JOINTLY-CONTROLLED OPERATION

	2004 HK\$'000	2003 HK\$'000
Assets recognised in respect of a jointly-controlled operation	—	1,634

On 24 August 2002, the Group entered into a joint venture agreement in the form of a jointly-controlled operation with 汕頭龍湖區欣源貿易公司(“欣源”) to manufacture, develop and distribute jointly a product line in the PRC. The Group and 欣源 have 55% and 45% participating interest in this joint venture respectively.

On 23 December 2003, both parties entered into a supplemental agreement whereby 欣源 agreed to transfer its profit-sharing interest in the product line and related plant and machinery with cost of HK\$5,081,000 to the Group for a guaranteed return of HK\$13,282,200 (equivalent to RMB14,100,000) (the “Transfer”). It is payable by 12 half-yearly installments.

Details of the payment schedule is set out below:

Date	Number of instalment and amount	Amount HK\$'000
July 2004 to January 2007	6 half-yearly instalments of HK\$1,271,700 (equivalent to RMB1,350,000) each	7,630
July 2007 to January 2010	6 half-yearly instalments of HK\$942,000 (equivalent to RMB1,000,000) each	5,652
		<u>13,282</u>

Following the Transfer, the risks and rewards of ownership of the product line passed to the Group. The aforementioned plant and machinery of HK\$5,081,000 were accounted for as additions to fixed assets during the year with the same amount credited as deferred income. The deferred income is recognised to the income statement over the terms of guaranteed period of six years.

Notes to Financial Statements

For the Year ended 31 July 2004

18. INTEREST IN AN ASSOCIATE

	2004 HK\$'000	2003 HK\$'000
Share of net assets	<u>9,583</u>	<u>8,134</u>

Particulars of the associate are as follows:

Name	Business structure	Place of establishment and operations	Percentage of ownership interest attributable to the Group		Principal activities
			2004	2003	
Chengdu Mt. Green Li Kong Medical Technology Co. Limited*	Corporate	PRC	30.94	30.94	Manufacture and sales of human drugs infusion medicine

* Not audited by PKF

19. LONG TERM INVESTMENTS

	2004 HK\$'000	2003 HK\$'000
Unlisted equity investments, at cost	<u>4,420</u>	<u>4,420</u>

20. INVENTORIES

	2004 HK\$'000	2003 HK\$'000
Raw materials	14,468	17,416
Work in progress	152	–
Finished goods	<u>6,850</u>	<u>11,119</u>
	<u>21,470</u>	<u>28,535</u>

Notes to Financial Statements

For the Year ended 31 July 2004

21. TRADE RECEIVABLES

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

An aged analysis of the trade receivables as at the balance sheet date, based on payment due date and net of provisions, is as follows:

	2004 HK\$'000	2003 HK\$'000
Within 3 months	59,394	112,334
3 to 6 months	43,759	29,933
6 to 12 months	38,052	32,259
Over 1 year	27,831	3,631
	<u>169,036</u>	<u>178,157</u>

22. DEPOSITS, PREPAYMENTS AND OTHER RECEIVABLES

	Group		Company	
	2004 HK\$'000	2003 HK\$'000	2004 HK\$'000	2003 HK\$'000
Prepayments	9,629	8,356	44	75
Deposits and other debtors	32,549	10,887	-	1,078
Short term loans	-	11,588	-	11,588
	<u>42,178</u>	<u>30,831</u>	<u>44</u>	<u>12,741</u>

Notes to Financial Statements

For the Year ended 31 July 2004

23. PLEDGED DEPOSITS AND CASH AND CASH EQUIVALENTS

	Group		Company	
	2004 HK\$'000	2003 HK\$'000	2004 HK\$'000	2003 HK\$'000
Cash and bank balances	67,844	67,961	11	345
Time deposits	41,374	41,305	41,375	41,305
	109,218	109,266	41,386	41,650
Analysed as:				
Deposits pledged for				
– Notes payable	65,649	58,512	–	–
– Bank loans	–	5,000	–	5,000
	65,649	63,512	–	5,000
Cash and cash equivalents	43,569	45,754	41,386	36,650
	109,218	109,266	41,386	41,650

Bank balances and time deposits of approximately HK\$3,000 (2003: HK\$136,000) and HK\$41,374,000 (2003: HK\$36,305,000) respectively are deposited with a related company of the Group, which is a bank.

Notes to Financial Statements

For the Year ended 31 July 2004

24. BANK AND OTHER BORROWINGS

	Group		Company	
	2004	2003	2004	2003
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Bank loans				
Secured (note 24(a))	110,394	108,816	–	10,000
Unsecured	65,563	77,611	–	–
	<u>175,957</u>	<u>186,427</u>	<u>–</u>	<u>10,000</u>
Other loans				
Secured (note 24(b))	2,449	2,449	–	–
Unsecured	6,919	7,518	–	–
	<u>9,368</u>	<u>9,967</u>	<u>–</u>	<u>–</u>
Convertible note, unsecured (note 24(c))	<u>26,741</u>	<u>26,741</u>	<u>26,741</u>	<u>26,741</u>
	212,066	223,135	26,741	36,741
Repayable:				
Within one year and shown under current liabilities				
Bank loans	155,308	186,427	–	10,000
Other loans	9,368	9,967	–	–
Convertible note	26,741	–	26,741	–
	<u>191,417</u>	<u>196,394</u>	<u>26,741</u>	<u>10,000</u>
In the second year and shown under non-current liabilities				
Bank loans	20,649	–	–	–
Convertible note	–	26,741	–	26,741
	<u>20,649</u>	<u>26,741</u>	<u>–</u>	<u>26,741</u>
	212,066	223,135	26,741	36,741

Notes to Financial Statements

For the Year ended 31 July 2004

24. BANK AND OTHER BORROWINGS (continued)

- (a) The bank loans are secured by:
- (i) mortgages over the Group's leasehold land and buildings which had an aggregate net book value at the balance sheet date of approximately HK\$64,413,000 (2003: HK\$68,337,000);
 - (ii) mortgages over the Group's plant and machinery which had an aggregate net book value at the balance sheet date of approximately HK\$29,290,000 (2003: HK\$35,232,000); and
 - (iii) bank deposits of the Company's director Mr. Wong Sai Wa of approximately HK\$942,000 (2003: the Group's deposits of HK\$5,000,000).
- (b) The other loan is secured by the Group's certain leasehold land and buildings, bears interest at 10% (2003: 10%) per annum and is repayable on demand.
- (c) The redeemable convertible note (the "Convertible Note") is unsecured, held by the Company's immediate holding company, Concord Pharmaceutical Technology (Holdings) Limited ("CPT") and bears interest at 3% per annum. CPT is wholly owned by director Mr. Wong Sai Chung.

The Convertible Note, which is transferable in whole (but not in part), confers the right on the holder to convert such note into shares of the Company at a conversion price of HK\$0.55 per share. The conversion period is from 10 October 2001 to 22 March 2004. The exercise in full of the conversion right would, under the present capital structure of the Company, result in the issue of approximately 48,619,564 additional ordinary shares of HK\$0.05 each.

The Convertible Note may be converted in full or in part (in amounts of not less than HK\$2 million on each conversion) of the principal amount thereof; any new shares issued as a result of the exercise of the conversion right attaching to the Convertible Note shall rank pari passu in all respects with the existing shares. The holder of the Convertible Note is not entitled to attend or vote at any general meeting of the Company.

CPT has given an undertaking to the Stock Exchange that it will not exercise the conversion attaching to the Convertible Note which may result in the public holding of the shares falling below 20%.

On 27 October 2003, the maturity date of the Convertible Note has been extended from 22 March 2004 to 22 March 2005 and is interest-free for such extension period.

Notes to Financial Statements

For the Year ended 31 July 2004

25. NOTES PAYABLE

As at 31 July 2004, the Group's notes payable were secured by the Group's bank deposit of approximately HK\$65,649,000 (2003: HK\$58,512,000).

26. TRADE PAYABLES

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

	2004 HK\$'000	2003 HK\$'000
Within 3 months	26,831	32,655
3 to 6 months	27,979	15,138
6 to 12 months	10,683	8,328
Over 1 year	16,597	10,081
	<u>82,090</u>	<u>66,202</u>

27. AMOUNTS DUE TO DIRECTORS

(a) The Group

The amounts due to directors Mr. Wong Sai Chung and Mr. Wong Sai Wa are interest-free, unsecured and repayable on demand.

(b) The Company

The amount due to a director Mr. Wong Sai Chung is interest-free, unsecured and repayable on demand.

28. SHARE CAPITAL

	2004 HK\$'000	2003 HK\$'000
Shares		
Authorised:		
1,000,000,000 ordinary shares of HK\$0.05 each	<u>50,000</u>	<u>50,000</u>
Issued and fully paid:		
500,000,000 shares of HK\$0.05 each	<u>25,000</u>	<u>25,000</u>

Share options

The details of share option schemes operated by the Company are set out in note 29 to the financial statements.

Notes to Financial Statements

For the Year ended 31 July 2004

29. SHARE OPTION SCHEMES

(a) Share Option Scheme

The Company operates a share option scheme (the “Scheme”) for the purpose of providing incentives and rewards to eligible participants who contribute to the success of the Group’s operations. Eligible participants of the Scheme include full-time employees and executive directors of the Company and any of its subsidiaries. The Scheme became effective on 23 March 2001 and, unless otherwise cancelled or amended, will remain in force for ten years from that date.

Options granted are exercisable at any time after the first anniversary of the grant of the option and during a period to be notified by the board of directors to each grantee, such period of time being not less than three years and not more than ten years from the date of grant of the options, but each shall lapse if the relevant grantee ceases to be employed by the relevant companies.

The maximum number of unexercised share options currently permitted to be granted under the Scheme is an amount, upon their exercise, not exceeding 10% of the entire issued share capital of the Company as at the end of the first day on which the dealings of the Company’s shares commenced on the GEM or 30% of the entire issued share capital of the Company on the day of shareholders’ approval for the refreshment of the 10% limit stated above, as the case may be. In determining the said 30% limit, the following shares shall be excluded: (1) shares issued pursuant to the Scheme and any other share option schemes; (2) any pro-rata entitlements to subscribe for further shares issued in respect of those shares mentioned in (1) above. The maximum number of shares issuable under share options to each eligible participant in the Scheme is limited to 25% of the aggregate number of shares of the Company in issue under the Scheme at any time. Any further grant of share options in excess of this limit is subject to shareholders’ approval in a general meeting.

Share options granted to a director, chief executive or substantial shareholder of the Company, or to any of their associates, are subject to approval in advance by all the independent non-executive directors of the Company. In addition, where share options are proposed to be granted to a connected person who is also a substantial shareholder of the Company, or any of its associates, and the proposed grant of share options, when aggregate with the options already granted to such connected person in the past 12 months, would entitle him/her to receive more than 0.1% of the total issued shares of the Company for the time being and the value of which is in excess of HK\$5 million, then the proposed grant must be subject to shareholders’ approval in general meeting.

The offer of a grant of share options may be accepted within five business days from the date of the offer and upon payment of a nominal consideration of HK\$1 in total by the grantee.

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For the Year ended 31 July 2004

29. SHARE OPTION SCHEMES *(continued)*

(a) Share Option Scheme *(continued)*

The subscription price of a share in respect of any particular option granted under the Scheme shall be such price as the board of directors in its absolute discretion shall determine, save that such price will not be less than the highest of (i) the closing price of the Company's shares on the GEM as stated in the Stock Exchange's daily quotation sheet on the date of grant of the options; (ii) the average of the closing price of the Company's shares as stated in the Stock Exchange's daily quotation sheets for the five business days immediately preceding the date of grant of the options; and (iii) the nominal value of the share.

No option has been granted by the Company under the Scheme since its adoption.

Share options do not confer rights on the holders to dividends or to vote at shareholders' meetings.

(b) Pre-IPO Share Option Scheme

The terms of the Company's Pre-IPO Share Option Scheme (the "Pre-IPO Plan") adopted by the Company on 23 March 2001 are substantially the same as those under the Scheme except that:

- (i) the subscription price is HK\$0.55 per share; and
- (ii) save for the options which have been granted under the Pre-IPO Plan (see below), no further options will be offered or granted under the Pre-IPO Plan as the right to do so was terminated upon the listing of the Company's shares on the GEM on 10 April 2001.

Notes to Financial Statements

For the Year ended 31 July 2004

29. SHARE OPTION SCHEMES (continued)

(b) Pre-IPO Share Option Scheme (continued)

The following share options were outstanding under the Pre-IPO Plan during the year:

Name or category of participant	At 1.8.2003	Granted during the year	Exercised during the year	Lapsed during the year	Cancelled during the year	At 31.7.2004	(Note 1)	(Note 2)	(Note 2)
							Date of grant of share options	Exercise period of share options	Exercise price of share options HK\$
<i>Directors</i>									
Mr. Wong Sai Wa	3,200,000	-	-	-	-	3,200,000	23.3.2001	10.10.2001 to 22.3.2011	0.55
Mr. Kwan Kai Cheong	3,000,000	-	-	-	-	3,000,000	23.3.2001	10.10.2001 to 22.3.2011	0.55
	6,200,000	-	-	-	-	6,200,000			
Other employees	800,000	-	-	(400,000)	-	400,000	23.3.2001	10.10.2001 to 22.3.2011	0.55
	7,000,000	-	-	(400,000)	-	6,600,000			

(Note 3)

Notes:

- (1) The vesting period of the share options is from the date of the grant until the commencement of the exercise period.
- (2) The exercise price of the share options is subject to adjustment in the case of rights or bonus issues, or other similar changes in the Company's share capital.
- (3) The share options lapsed upon the termination of employment with an employee.

The exercise of the above 6,600,000 outstanding share options at the balance sheet date would, under the present capital structure of the Company, result in the issue of 6,600,000 additional ordinary shares of the Company and additional share capital of HK\$330,000 and share premium of HK\$3,300,000 (before issue expenses).

Share options do not confer rights on the holders to dividends or to vote at shareholders' meetings.

Notes to Financial Statements

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30. RESERVES

(a) The Group

The capital reserve arising from capitalisation of a loan represents the difference between the amount due to director Mr. Wong Sai Chung capitalised and the nominal value of shares issued by China Biotechnology Limited.

(b) The Company

	Share premium HK\$'000	Contributed surplus HK\$'000	Accumulated losses HK\$'000	Total HK\$'000
At 1 August 2002	17,992	42,876	(4,929)	55,939
Loss for the year	<u>—</u>	<u>—</u>	<u>(2,972)</u>	<u>(2,972)</u>
At 31 July 2003 and 1 August 2003	17,992	42,876	(7,901)	52,967
Loss for the year	<u>—</u>	<u>—</u>	<u>(3,499)</u>	<u>(3,499)</u>
At 31 July 2004	<u>17,992</u>	<u>42,876</u>	<u>(11,400)</u>	<u>49,468</u>

The contributed surplus represents the excess of the combined net asset value of the subsidiaries acquired pursuant to the reorganisation to rationalise the structure of the Group in preparation for the listing of the Company's shares on GEM over the nominal value of the Company's shares issued in exchange.

The Company had distributable reserves of approximately HK\$49,468,000 as at 31 July 2004. Under the Companies Law (Cap. 22 Law 3 of 1961, as consolidated and revised) of the Cayman Islands, the share premium is distributable to the shareholders of the Company, provided that immediately following the date on which the dividends is proposed to be distributed, the Company will be in a position to pay off its debts as they fall due in the ordinary course of business.

Notes to Financial Statements

For the Year ended 31 July 2004

31. NOTES TO THE CONSOLIDATED CASH FLOW STATEMENT

(a) Acquisition of a subsidiary during the year:

	2004 HK\$'000	2003 HK\$'000 (Restated)
Net assets acquired:		
Fixed assets	656	82,409
Intangible assets	6,924	–
Long term investments	–	3,224
Deferred tax asset	265	–
Inventories	1,065	16,035
Trade receivables	–	64,364
Other receivables	246	14,406
Cash and cash equivalents	31	26,762
Trade payables	–	(39,232)
Notes payable	–	(42,390)
Other payables and accruals	(1,751)	(33,303)
Interest-bearing bank and other loans	–	(85,601)
Deferred tax liability	–	(367)
Minority interests	(1,132)	(4,221)
	<u>6,304</u>	2,086
Goodwill arising on acquisition	<u>3,593</u>	11,328
	<u>9,897</u>	13,414
Satisfied by:		
Cash paid	7,655	13,414
Other payable	2,242	–
	<u>9,897</u>	13,414

Notes to Financial Statements

For the Year ended 31 July 2004

31. NOTES TO THE CONSOLIDATED CASH FLOW STATEMENT (continued)

An analysis of the net (outflow)/inflow of cash and cash equivalents in respect of the acquisition of a subsidiary is as follows:

	2004 HK\$'000	2003 HK\$'000
Cash consideration	(7,655)	(13,414)
Cash and cash equivalents acquired	<u>31</u>	<u>26,762</u>
Net (outflow)/inflow of cash and cash equivalents in respect of the acquisition of a subsidiary	<u>(7,624)</u>	<u>13,348</u>

(b) Disposal of a subsidiary during the year:

	2004 HK\$'000
Net liabilities disposed of:	
Cash and cash equivalents	9
Deferred tax liability	(30)
Minority interests	<u>(2,769)</u>
	(2,790)
Unamortised goodwill written off	188
Gain on disposal	<u>1,641</u>
	(961)
Satisfied by:	
Other payable	<u>(961)</u>

An analysis of the outflow of cash and cash equivalents in respect of the disposal of a subsidiary is as follows:

	2004 HK\$'000
Cash and cash equivalents disposed of	<u>9</u>

(c) Major non-cash transaction

As detailed in note 17 to the financial statements, certain plant and machinery amounting to HK\$5,081,000 was acquired under the Transfer without cash payment.

Notes to Financial Statements

For the Year ended 31 July 2004

32. CONTINGENT LIABILITIES

The Company and the Group did not have any significant contingent liabilities at the balance sheet date.

33. PLEDGE OF ASSETS

The details of the Group's assets which were pledged to secure the banking facilities and other borrowings granted to the Group are set out in notes 13 and 23 to 25 to the financial statements respectively.

34. OPERATING LEASE ARRANGEMENTS

As at 31 July 2004, the Group and the Company had outstanding commitments under non-cancellable operating leases for the use of land and buildings which fall due as follows:

	Group		Company	
	2004 HK\$'000	2003 HK\$'000	2004 HK\$'000	2003 HK\$'000
Within one year	<u>165</u>	<u>158</u>	<u>150</u>	<u>150</u>

Operating lease rentals represent rental payable by the Group and the Company for office premises. Leases are negotiated for an average term of three months to one year with fixed monthly rentals.

35. COMMITMENTS

As at 31 July 2004, the Group had the following capital commitments:

(a) Capital commitments

	2004 HK\$'000	2003 HK\$'000
Authorised and contracted for:		
Acquisition of plant and machinery	–	39
Acquisition of subsidiaries	–	<u>2,713</u>
	<u>–</u>	<u>2,752</u>

(b) Other commitments

Commitments under:		
Technology development	3,005	2,191
Guaranteed return (note 17)	<u>11,799</u>	–
	<u>14,804</u>	<u>2,191</u>

The Company did not have any commitments at the balance sheet date.

Notes to Financial Statements

For the Year ended 31 July 2004

36. CONNECTED AND RELATED PARTY TRANSACTIONS

Apart from the transactions as disclosed in notes 23, 24 and 27 to the financial statements, the Group had the following material transactions with its related parties during the year:

	Notes	2004 HK\$'000	2003 HK\$'000
Interest income received from a related company	(i)	149	429
Licence fee for office premises paid to Frank Union Limited	(ii)	600	600
Interest paid to Concord Pharmaceutical Technology (Holdings) Limited	(iii)	535	802

Mr. Wong Sai Chung, a director and beneficial shareholder of the Company, is also a director and beneficial shareholder of the above companies.

Notes:

- (i) *The interest income was generated from the deposits held by a related company, which is a bank. The interest rates on the bank accounts are similar to those given to other customers of the bank.*
- (ii) *The licence fee relates to the office premises used by the Group. The licence fee was charged at HK\$50,000 per month (2003: HK\$50,000 per month).*
- (iii) *The interest paid relates to the Convertible Note and was charged at 3% per annum. Further details of the Convertible Note are set out in note 24 to the financial statements.*

In the opinion of the directors, all the above transactions were conducted in the normal course of the Group's business.