

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

*(Incorporated in the Cayman Islands with limited liability)*

**THIRD QUARTERLY REPORT**

**2005**

*\* For identification purposes only*

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

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

## HIGHLIGHTS

- Turnover of the Group for the nine months ended 30 April 2005 amounted to approximately HK\$104,077,000, representing a decrease of approximately 21.6% as compared with that in the preceding year.
- Net loss attributable to shareholders for the nine months ended 30 April 2005 amounted to approximately HK\$57,309,000, including a provision for loss of approximately HK\$45,499,000 incurred for the disposal of discontinuing operations.
- Loss per share amounted to approximately HK11.46 cents for the nine months ended 30 April 2005.
- The Directors do not recommend the payment of any interim dividend for the nine months ended 30 April 2005.
- The Group has decided to dispose of all its human drugs and packaging materials businesses and thereafter focuses its operations on veterinary drugs and animal vaccines. Further to the disposal of Chengdu Mt. Green and Sichuan Future announced on 24 December 2004, the Group is in the process of disposing its entire 51.05% equity interest in Sichuan Shule to an independent third party (the "Proposed Disposal"). The completion of the Proposed Disposal is subject to the completion of certain procedures. Details of the Proposed Disposal will be announced as soon as practicable.

## RESULTS

The board of directors (the “Board”) of China Medical Science Limited (the “Company”) presents the unaudited consolidated results of the Company and its subsidiaries (collectively, the “Group”) for the three months and nine months ended 30 April 2005, together with the comparative unaudited figures for the corresponding periods of the previous financial year are as follows:

### Consolidated Income Statement- Unaudited

	Note	For the three months ended 30 April		For the nine months ended 30 April	
		2005 HK\$'000	2004 HK\$'000 (Restated)	2005 HK\$'000	2004 HK\$'000 (Restated)
Turnover					
Continuing operations	2	5,492	5,731	20,934	16,745
Discontinuing operations	2	14,932	31,282	83,143	115,943
		<u>20,424</u>	<u>37,013</u>	<u>104,077</u>	<u>132,688</u>
Cost of sales		(13,925)	(32,150)	(79,035)	(108,825)
Gross profit		6,499	4,863	25,042	23,863
Other revenue & gains		1,077	847	2,441	1,893
Selling and distribution costs		(4,272)	(3,388)	(11,812)	(9,736)
General and administrative expenses		(4,912)	(4,930)	(15,806)	(13,171)
Other operating expenses		(292)	(5,181)	(3,970)	(8,841)
Provision for loss on disposal of discontinuing operations	3	(26,019)	–	(45,499)	–
<b>LOSS FROM OPERATING ACTIVITIES</b>		<u>(27,919)</u>	<u>(7,789)</u>	<u>(49,604)</u>	<u>(5,992)</u>
Finance costs		(1,865)	(5,163)	(10,984)	(13,313)
Share of result of an associate		–	370	1,914	963
		<u>–</u>	<u>370</u>	<u>1,914</u>	<u>963</u>
<b>LOSS BEFORE TAX</b>		<u>(2,879)</u>	<u>(1,943)</u>	<u>(2,593)</u>	<u>(4,301)</u>
Continuing operations		(2,879)	(1,943)	(2,593)	(4,301)
Discontinuing operations		(26,905)	(10,639)	(56,081)	(14,041)
Tax expense	4	–	–	–	–
Continuing operations		–	–	–	–
Discontinuing operations		–	–	(101)	–
		<u>–</u>	<u>–</u>	<u>(101)</u>	<u>–</u>
<b>LOSS BEFORE MINORITY INTERESTS</b>		<u>(29,784)</u>	<u>(12,582)</u>	<u>(58,775)</u>	<u>(18,342)</u>
Minority interests		(316)	1,936	1,466	1,465
		<u>(30,100)</u>	<u>(10,646)</u>	<u>(57,309)</u>	<u>(16,877)</u>
<b>NET LOSS ATTRIBUTABLE TO SHAREHOLDERS</b>		<u>(30,100)</u>	<u>(10,646)</u>	<u>(57,309)</u>	<u>(16,877)</u>
<b>LOSS PER SHARE</b>	5				
– Basic		6.02 cents	2.13 cents	11.46 cents	3.38 cents
– Diluted		N/A	N/A	N/A	N/A
		<u>6.02 cents</u>	<u>2.13 cents</u>	<u>11.46 cents</u>	<u>3.38 cents</u>
		<u>N/A</u>	<u>N/A</u>	<u>N/A</u>	<u>N/A</u>

Notes:

## 1. Basis of presentation

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

The principal accounting policies adopted in preparing the unaudited consolidated results are consistent with those used in the annual financial statements for the year ended 31 July 2004 of the Group.

## 2. Turnover

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

An analysis of turnover is as follows:

	For the three months ended 30 April		For the nine months ended 30 April	
	2005 HK\$’000	2004 HK\$’000	2005 HK\$’000	2004 HK\$’000
Continuing operations				
Sale of veterinary drugs and animal vaccines	5,492	5,731	20,934	16,745
Discontinuing operation				
Sale of human drugs	14,932	26,074	78,812	100,965
Sale of packaging materials	–	5,208	4,331	14,978
	<u>14,932</u>	<u>31,282</u>	<u>83,143</u>	<u>115,943</u>
	<u><u>20,424</u></u>	<u><u>37,013</u></u>	<u><u>104,077</u></u>	<u><u>132,688</u></u>

## 3. Discontinuing operations

The Group has decided to dispose of all its human drugs and packaging materials businesses and thereafter focuses its operations on veterinary drugs and animal vaccines. Further to the disposal of Chengdu Mt. Green and Sichuan Future announced on 24 December 2004, the Group is in the process of disposing its entire 51.05% equity interest in Sichuan Shule to an independent third party (the “Proposed Disposal”). The completion of the Proposed Disposal is subject to the completion of certain procedures. Details of the Proposed Disposal will be announced as soon as practicable.

The turnover, other revenue, expenses and results of the segments of packaging materials and human drugs, included in the Group's unaudited consolidated income statement for the nine months ended 30 April 2005 and 30 April 2004 respectively are as follows:

	Packaging materials		Human drugs		Total	
	2005	2004	2005	2004	2005	2004
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Turnover	4,331	14,978	78,812	100,965	83,143	115,943
Cost of sales	<u>(3,841)</u>	<u>(13,051)</u>	<u>(61,750)</u>	<u>(83,806)</u>	<u>(65,591)</u>	<u>(96,857)</u>
Gross profit	490	1,927	17,062	17,159	17,552	19,086
Selling and distribution costs	(312)	(651)	(7,865)	(7,181)	(8,177)	(7,832)
General and administrative expenses	(1,127)	(1,851)	(9,276)	(5,733)	(10,403)	(7,584)
Other operating expenses	(335)	(491)	(2,048)	(7,350)	(2,383)	(7,841)
Provision for loss on disposal of discontinuing operations*	<u>(23,109)</u>	<u>–</u>	<u>(22,390)</u>	<u>–</u>	<u>(45,499)</u>	<u>–</u>
Segment results	<u><u>(24,393)</u></u>	<u><u>(1,066)</u></u>	<u><u>(24,517)</u></u>	<u><u>(3,105)</u></u>	<u><u>(48,910)</u></u>	<u><u>(4,171)</u></u>
Interest and unallocated income					<u>1,348</u>	<u>1,065</u>
Loss from operating activities					(47,562)	(3,106)
Finance costs					(10,433)	(11,898)
Share of result of an associate					<u>1,914</u>	<u>963</u>
Loss before tax					(56,081)	(14,041)
Tax expense					<u>(101)</u>	<u>–</u>
Loss before minority interests					(56,182)	(14,041)
Minority interests					<u>1,414</u>	<u>1,232</u>
Net loss attributable to shareholders					<u><u>(54,768)</u></u>	<u><u>(12,809)</u></u>

\* Including the provision for written off of positive goodwill of approximately HK\$16,021,000.

#### 4. Tax expense

No provision for Hong Kong profits tax has been made, as the Group had no assessable profits arising in Hong Kong for the nine months ended 30 April 2005 (2004: Nil). Taxes on profits assessable elsewhere have been calculated at the rates of tax prevailing in the countries in which the Group operates, based on existing legislation, interpretations and practices in respect thereof.

The deferred tax credit of approximately HK\$1,000 and approximately HK\$3,000 recognised for the three months and nine months ended 30 April 2005 respectively (three months and nine months ended 30 April 2004: approximately HK\$4,000 and approximately HK\$12,000 respectively) represents the movement for temporary difference arising from the acquisition of subsidiaries.

#### 5. Loss per share

The calculation of basic loss per share for the three months and nine months ended 30 April 2005 was based on the unaudited net loss attributable to shareholders of approximately HK\$30,100,000 and approximately HK\$57,309,000 respectively (three months and nine months ended 30 April 2004: approximately HK\$10,646,000 and approximately HK\$16,877,000 respectively) and the weighted average number of 500,000,000 for the three months and nine months ended 30 April 2005 (three months and nine months ended 30 April 2004: 500,000,000) ordinary shares in issue during the period.

No diluted loss per share are presented for the three months and nine months ended 30 April 2005 and the three months and nine months ended 30 April 2004 respectively as the potential ordinary share issuable under the Company's share option scheme had an anti-dilutive effect on the basic loss per share for the relevant periods.

#### 6. Reserves

	Share premium <i>HK\$'000</i>	Capital reserve <i>HK\$'000</i>	Exchange fluctuation reserve <i>HK\$'000</i>	Retained profits <i>HK\$'000</i>	Total <i>HK\$'000</i>
At 1 August 2003	17,992	27,104	25	49,615	94,736
Net loss for the period	<u>-</u>	<u>-</u>	<u>-</u>	<u>(16,877)</u>	<u>(16,877)</u>
At 30 April 2004	<u>17,992</u>	<u>27,104</u>	<u>25</u>	<u>32,738</u>	<u>77,859</u>
At 1 August 2004	17,992	27,104	25	5,824	50,945
Net loss for the period	<u>-</u>	<u>-</u>	<u>-</u>	<u>(57,309)</u>	<u>(57,309)</u>
At 30 April 2005	<u>17,992</u>	<u>27,104</u>	<u>25</u>	<u>(51,485)</u>	<u>(6,364)</u>

## **DIVIDEND**

The Directors do not recommend the payment of any interim dividend for the nine months ended 30 April 2005 (2004: Nil).

## **BUSINESS REVIEW AND OUTLOOK**

### **FINANCIAL REVIEW**

For the nine months ended 30 April 2005, the turnover of the Group amounted to HK\$104,077,000, representing a decrease of approximately 21.6%, as compared with that of the corresponding period in 2004. The competition from severe price volatility in infusion medicine market and also in packaging materials market was the key factor affecting the business performance of the Group for the period under review. The decrease in turnover was also accelerated by the cease of operations of Chengdu Mr. Green and Sichuan Future. After the substantial provision for loss on disposal of discontinuing operations of approximately HK\$45,499,000 made during the period, the Group recorded a loss for the nine-months period of approximately HK\$57,309,000 (2004: approximately HK\$16,877,000).

### **OPERATION REVIEW**

As stated earlier, the Group has decided to dispose of all its human drugs and packaging materials businesses and thereafter focuses its operations on veterinary drugs and animal vaccines.

#### **Continuing operation**

##### *– Veterinary drug and animal vaccines*

During the nine-months period under review, the turnover of Chengdu Yuan Heng increased from approximately HK\$15,110,000 last year to approximately HK\$20,052,000 for the corresponding period this year, representing an increase of 32.7%. The increase was mainly the result of a change in sales mix in favour of new products with higher profit margin and also contribution from the original equipment manufacturer (“OEM”) products.

To pursue a more comprehensive sales network in the PRC, Chengdu Yuan Heng during the period under review has been commencing its strategic marketing program “Thousand County Project” to build up its market intelligence and products distribution system in the principal livestock producing counties. Consistent with its new marketing program, the company enforced the regional sales management system during the period under review to ensure effective control over contractual dealers in various regions. Chengdu Yuan Heng also adjusted the composition of sales team by recruiting local experienced sales persons in certain regions that more effectively enhanced overall talent resources.



## **Discontinuing operations**

### *– Human drugs*

Despite the effort and resources allocated by the Group to improve the productivity and introduce value-added products, the intense competition in the infusion medicine market continues to push the average unit price of the products downward. As a result, our human drugs segment has been operating under a tight cash-flow, which was aggravated by the substantial short term liabilities. In view of the foregoing, the Group has decided to dispose of the human drugs segment where Sichuan Shule and Chengdu Mt. Green operate.

### *– Packaging materials*

In addition to the intensified competition causing the decrease of the selling price of our products, the profit margin was also adversely impacted by the rising cost of raw materials. As previously announced, the Group arrived at the conclusion that it would be in the interest of the Group to dispose of this loss making segment.

## **Research and Development**

The research and development projects undertaken by Chengdu Yuan Heng are progressing well. During the period under review, Chengdu Yuan Heng, worked in conjunction with Sichuan Agriculture University and Southwestern Agriculture University for the development of new products.

For the veterinary drug, about 18 products had obtained pharmaceutical registration during the period under review, namely Macleayae Injection, Compound Sulfamonomethoxine Sodium LongActing Injection, Compound Enrofloxacin Injection, Benzylpenicillin Potassium for Injection (1.0g), Gentamycin Sulfate Injection 5ml:0.2g, Enrofloxacin and Sulfamonomethoxine Injection, Compound Apramycin Sulfate Injection 5ml, Benzathine Benzylpenicillin for Injection (0.6 million), Benzathine Benzylpenicillin for Injection (1.2 million), Digtoxacin Hydrochloride Injection 10ml, Compound Sulfadiazine Sodium Injection 10ml, Saragtoxacm Hydrochloride Injection 10ml: 0.1g, Saragtoxacm Hydrochloride Injection 10ml, Cloxacillin Sodium for Injection (0.5g), Ceftiofur Sodium for Injection (0.25g), Ceftiofur Sodium for Injection (1.0g), Enrofloxacin and Sulfamonomethoxine Injection (1.0g) and Compound Ofloxacin Injection 10ml.

## OUTLOOK

As stated earlier, the Group has decided to dispose of all its human drugs and packaging materials businesses and thereafter focuses its operations on veterinary drugs and animal vaccines.

When the disposal of all discontinuing operations is completed, the Group would be in a better financial position to pursue on the opportunities in the area of veterinary drugs and animal vaccines.

## COMPETING INTEREST

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

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

As at 30 April 2005, the interests or short positions of the directors and chief executives in the shares, underlying shares and debentures of the Company or any of its associated corporations (within the meaning of Part XV of the Securities and Futures Ordinance ("SFO")) which were notified to the Company and The Stock Exchange of Hong Kong Limited (the "Stock Exchange") pursuant to Division 7 and 8 of Part XV of the SFO (including interests or short positions which they were taken or deemed to have under such provisions of the SFO), or which were required, 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 corporation	Ordinary shares	400,000,000 shares	80%	a
Mr. Wong Sai Wa	Directly beneficially owned	Share options	3,200,000 share options	0.64%	b
Mr. Kwan Kai Cheong	Directly beneficially owned	Share options	3,000,000 share options	0.60%	b

*Notes:*

- (a) These shares are registered in the name of CPT, a wholly-owned subsidiary of Concord Business Management Limited (“CBM” hereinafter). As at 30 April 2005, 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) Pursuant to the terms of the Company’s Pre-IPO Share Option Scheme (the “Pre-IPO Plan”) adopted by the Company on 23 March 2001, the Company has granted the above options to the directors to subscribe for shares in the Company at any time from 10 October 2001 up to and including 22 March 2011 at an exercise price of HK\$0.55 per share. The exercise period of the Pre-IPO Plan is set out under the paragraph headed “Share Option Schemes” below. Details of the Pre-IPO Plan are set out in the Prospectus.
- (c) Convertible Note in the Principal amount of HK\$26,740,760 issued by the Company to CPT on 23 March 2001 has been repaid by the Company to CPT in full by 22 December 2004.

Save as disclosed herein, as at 30 April 2005, none of the directors or chief executives of the Company has short positions in the shares or underlying shares of equity derivatives of the Company.

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

## **SHARE OPTION SCHEMES**

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

Pursuant to the Pre-IPO Plan, five employees of the Group (including two executive Directors) were conditionally granted options on 23 March 2001 to subscribe for an aggregate of 7,400,000 shares, which upon exercise in full will result in issue of 7,400,000 additional ordinary shares of HK\$0.05 each for aggregate proceeds of HK\$4,070,000 before the related shares issue expense. All of these options have a duration of 10 years from the date of grant of the options, and each option is exercisable in accordance with the terms of issue after 6 months from the date of listing of the shares on GEM, but each shall lapse if the relevant grantee ceases to be employed by the relevant companies. The options of 800,000 shares granted to the

ex-employees were cancelled due to their resignation from the Group. Accordingly, as at 30 April 2005, the number of share options granted to the employees remained at 6,600,000 shares. An aggregate amount of HK\$3,630,000 will be generated if all share options are fully exercised. During the nine months ended 30 April 2005, none of the directors or employees of the Company had exercised any share options and no allotment or issue of shares was made pursuant to the Pre-IPO Plan.

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

## **SUBSTANTIAL SHAREHOLDERS' INTERESTS**

As at 30 April 2005, 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	Corporation	Ordinary shares	400,000,000 shares	80%	a and b
CBM	Through controlled corporation	Ordinary shares	400,000,000 shares	80%	a and b

#### *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) Convertible Note in the Principal amount of HK\$26,740,760 issued by the Company to CPT on 23 March 2001 has been repaid by the Company to CPT in full by 22 December 2004.

Save as disclosed above, as at 30 April 2005, the directors or chief executives of the Company were not aware of any other person (other than directors or chief executives of the Company) who had an interest or short position in the shares or underlying shares of the Company which would fall to be disclosed to the Company under the provisions of Divisions 2 and 3 of Part XV of the SFO, or who was interested in 10% or more of the nominal value of any class of share capital carrying rights to vote in all circumstances at general meeting of any other member of the Group.

#### **AUDIT COMMITTEE**

The Company set up an audit committee on 23 March 2001 with written terms of reference in compliance with the requirements as set out in Rules 5.28, 5.29 and 5.30 of the GEM Listing Rules. The audit committee has 3 members, namely Mr. Chow Wai Ming, Mr. Garry Alides Willinge and Mr. Lai Chik Fan. The work undertaken by the audit committee are to review the Company's annual report and financial statements, half-yearly report and quarterly reports and to provide advice and comment thereon to the board of directors. The audit committee will also be responsible for reviewing and supervising the financial reporting process and internal control procedures of the Group.

#### **COMPLIANCE WITH BOARD PRACTICE AND PROCEDURES**

During the period under review, the Company was in compliance with the Board Practices and Procedures as set out in Rules 5.34 to 5.45 of the GEM Listing Rules, which applied before the amendment of the GEM Listing Rules relating to the Code on Corporate Governance Practices and Rules on Corporate Governance Report on 1 January 2005. The Code has become effective for accounting periods commencing on or after 1 January 2005. The Company will prepare a Corporate Governance Report in accordance with Rule 18.44 of the GEM Listing Rules for the financial year ending 31 July 2006.

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

During the nine months ended 30 April 2005, neither the Company nor any of its subsidiaries had purchased, sold or redeemed any of the Company's listed securities.

By Order of the Board  
**China Medical Science Limited**  
**Yu Ling Ling**  
*Company Secretary*

Hong Kong, 14 June, 2005

As at the date of this report, the Board comprises three executive directors, namely Mr. Wong Sai Wa, Mr. Kwan Kai Cheong, and Mr. Wong Fei Fei; and three independent non-executive directors, namely Mr. Chow Wai Ming, Mr. Lai Chik Fan and Mr. Garry Alides Willinge.