

CHINA MEDICAL SCIENCE LIMITED

中華藥業有限公司*

(Incorporated in the Cayman Islands with limited liability)

FIRST QUARTERLY REPORT

2005/2006

** 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 three months ended 31 October 2005 amounted to approximately HK\$35,808,000, representing a decrease of approximately 22.4% as compared with that in the preceding year.
- Loss attributable to shareholders for the three months ended 31 October 2005 amounted to approximately HK\$1,434,000.
- Loss per share amounted to approximately HK0.29 cents for the three months ended 31 October 2005.
- The Directors do not recommend the payment of any interim dividend for the three months ended 31 October 2005.

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 ended 31 October 2005, together with the comparative unaudited figures for the corresponding period of the preceding year are as follows:

		For the three months ended 31 October	
	<i>Note</i>	2005 <i>HK\$'000</i>	2004 <i>HK\$'000</i> (restated)
Turnover			
Continuing operations	2	35,808	43,450
Discontinued operations	2	—	2,674
		<u>35,808</u>	<u>46,124</u>
Cost of sales		(23,285)	(33,991)
Gross profit		12,523	12,133
Other revenue		810	807
Selling and distribution costs		(5,339)	(6,083)
General and administrative expenses		(5,735)	(6,285)
Other operating expenses		(726)	(1,468)
		<u>1,533</u>	<u>(896)</u>
PROFIT/(LOSS) FROM OPERATING ACTIVITIES		1,533	(896)
Finance costs		(3,335)	(4,578)
Share of result of an associate		—	582
		<u>—</u>	<u>582</u>
LOSS BEFORE TAX		(1,802)	(2,872)
Continuing operations		(1,802)	(2,872)
Discontinued operations		—	(2,020)
		<u>(1,802)</u>	<u>(4,892)</u>
Tax expense	4	(120)	(83)
Continuing operations		(120)	(83)
Discontinued operations		—	—
		<u>(120)</u>	<u>(83)</u>
LOSS AFTER TAX		<u>(1,922)</u>	<u>(4,975)</u>
Attributable to:			
Equity holders of the Company		(1,434)	(4,848)
Minority interests		(488)	(127)
		<u>(1,922)</u>	<u>(4,975)</u>
LOSS PER SHARE ATTRIBUTABLE TO SHAREHOLDERS OF THE COMPANY	5		
– Basic		<u>(0.29 cents)</u>	<u>(0.97 cents)</u>
– Diluted		<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 new and revised Hong Kong Financial Reporting Standards and Hong Kong Accounting Standards (collectively referred to as “HKFRSs”) issued by the Hong Kong Institute of Certified Public Accountants (“HKICPA”), which are effective for accounting periods beginning on or after 1 January 2005. The adoption of the new HKFRSs has resulted in changes to the Group’s accounting policies in the following areas that have an effect on how the results for current or prior accounting periods are prepared and presented.

HKAS 1 Presentation of Financial Statements and HKAS 27 Consolidated and Separate Financial Statements

The adoption of HKAS 1 and HKAS 27 affects certain presentation and disclosure of the accounts. According to HKAS 1 and HKAS 27, minority interests at the balance sheet are presented in the consolidated balance sheet within equity, separately from the equity attributable to the equity holders of the Company, and minority interests in the results of the Group for the period are presented on the face of the consolidated income statement as an allocation of the total profit and loss for the period between minority interests and the equity holders of the Company.

HKFRS 3 Business Combinations

The adoption of HKFRS 3 has resulted in a change in accounting policy for goodwill and negative goodwill. In prior years, goodwill was amortised on a straight line basis over a period of not exceeding 20 years and assessed for the impairment at each balance sheet date. Negative goodwill was presented as a deduction from assets and released to income based on an analysis of the circumstances from which the balance resulted.

In accordance with the provision of HKFRS 3, the Group ceased amortisation of goodwill from 1 August 2005 onwards and goodwill will be tested for impairment at least annually or in the financial year in which the acquisition takes place. The Group has derecognised all negative goodwill previously presented as a deduction from assets with a corresponding increase to retained earnings.

HKFRS 5 Non-current Assets Held for Sale and Discontinued Operations

The adoption of HKFRS 5 affects certain presentation and disclosure of the accounts. The HKFRS 5 changes the timing of the classification of an operation as discontinued. In accordance with HKFRS 5, the Company classifies an operation as discontinued at the date as the Group has disposed of the operation.

2. Turnover

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

An analysis of the Group's turnover is as follows:

	For the three months ended 31 October	
	2005 HK\$'000	2004 HK\$'000
Continuing operations (including discontinuing operations)		
Sale of veterinary drugs	6,743	7,563
Sale of human drugs	29,065	35,887
	<u>35,808</u>	<u>43,450</u>
Discontinued operations		
Sale of packaging materials	—	2,674
	<u>35,808</u>	<u>46,124</u>

3. Discontinuing operations

On 20 May 2005, Chengdu Viking Yuen Heng, an indirectly 91% owned subsidiary of the Company has entered into the Equity Interest Transfer Agreement with an independent third party for the disposal of the 51.05% equity interest in Sichuan Shule together with its subsidiary for a consideration of RMB1.00. Upon completion of the disposal of Sichuan Shule and its subsidiary, the Group would discontinue its development, production, sales and distribution of human drugs business.

4. Tax expenses

No provision for Hong Kong profits tax has been made, as the Group had no assessable profits arising in Hong Kong for the three months ended 31 October 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 recognised for the three months ended 31 October 2004 represents the movement in temporary difference arising from the acquisition of subsidiaries. There is no deferred tax credit recognised for the three months ended 31 October 2005.

5. Loss per share

The calculation of basic loss per share for the three months ended 31 October 2005 was based on the unaudited net loss attributable to shareholders of approximately HK\$1,434,000 (2004: approximately HK\$4,848,000) and the weighted average number of 500,000,000 (2004: 500,000,000) ordinary shares in issue during the period.

No diluted loss per share are presented for the three months ended 31 October 2005 and 2004 respectively as there were no dilutive potential shares.

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 2004	17,992	27,104	25	5,824	50,945
Net loss for the period	<u>–</u>	<u>–</u>	<u>–</u>	<u>(4,848)</u>	<u>(4,848)</u>
At 31 October 2004	<u>17,992</u>	<u>27,104</u>	<u>25</u>	<u>976</u>	<u>46,097</u>
At 1 August 2005	17,992	27,104	828	(57,736)	(11,812)
Effects of change in accounting policies	<u>–</u>	<u>–</u>	<u>–</u>	<u>4,745</u>	<u>4,745</u>
As restated	<u>17,992</u>	<u>27,104</u>	<u>828</u>	<u>(52,991)</u>	<u>(7,067)</u>
Exchange difference arising on translation of financial statements of PRC subsidiaries	–	–	55	–	55
Net loss for the period	<u>–</u>	<u>–</u>	<u>–</u>	<u>(1,434)</u>	<u>(1,434)</u>
At 31 October 2005	<u>17,992</u>	<u>27,104</u>	<u>883</u>	<u>(54,425)</u>	<u>(8,446)</u>

DIVIDEND

The Directors do not recommend the payment of any interim dividend for the three months ended 31 October 2005 (2004: Nil).

BUSINESS REVIEW AND OUTLOOK

FINANCIAL REVIEW

For the three months ended 31 October 2005, the Group recorded a turnover of approximately HK\$35,808,000. A decrease in turnover of approximately 22.4% as compared to approximately HK\$46,124,000 that was recorded in the preceding year. The decrease in turnover was mainly attributable to the disposal of Chengdu Mt. Green and Sichuan Future during the financial year ended 31 July 2005. The loss after tax attributable to the equity holders of the Company for the three months ended 31 October 2005 was approximately HK\$1,434,000 (2004: approximately HK\$4,848,000).

OPERATION REVIEW

– Veterinary drug and animal vaccines

During the three-months period under review, the turnover of Chengdu Yuan Heng amounted to approximately HK\$6,558,000, representing a decrease of approximately 13.8% as compared with the corresponding period in the preceding year. Unstable contributions from the original equipment manufacturer (“OEM”) products and keen competition from non-GMP compliance manufacturers in the veterinary drug market have an adverse impact on the turnover for the period under review.

Chengdu Yuan Heng during the period under review still uphold its strategic marketing program “Thousand County Project” to build up its market intelligence and products distribution system in the principal livestock producing counties. In order to ensure more comprehensive sales network in the PRC, the company has instituted the regional sales management system across the principal counties to ensure effective planning and control over contractual dealers in various regions.

– Human drugs

In view of focusing the development in a more promising veterinary pharmaceutical market, the Group decided to dispose of the human drugs business. The Group had entered into Equity Interest Transfer Agreements with independent third parties to dispose of its entire 51.05% equity interest in Sichuan Shule. The completion of the said disposal is subject to the completion of certain procedures, mainly involving the issuance of a circular in accordance with the GEM Listing Rules.

Research and Development

Chengdu Yuan Heng, during the period under review, continued in collaboration with Sichuan Agriculture University and Southwestern Agriculture University for developing of new products.

For the veterinary drug, about five products had obtained pharmaceutical registration during the period under review, namely Antondini Injection 10ml, Dexamethason Sodium Phosphate Injection 1ml:2mg, Dexamethasone Sodium Phosphate Injection 1ml:1mg, Antondini Injection 5ml and Dexamethasone Sodium Phosphate Injection 1ml:5mg.

OUTLOOK

Following the completion of the disposal of the businesses of the human drugs segment and packaging materials segment, the Group will consolidate and focus its resources exclusively in the more profitable veterinary drug business segment. In addition, the Group is moving ahead to source business opportunities with development potential, by taking advantage of its existing network in the veterinary drug market, so as to increase the revenue stream of the Group.

COMPETING INTEREST

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

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

As at 31 October 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 5.68 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 of shares/equity derivatives held	Percentage of the Company's issued share capital	Note
Mr. Wong Sai Wa	Directly beneficially owned	Share options	3,200,000 share options	0.64%	(a)
Mr. Kwan Kai Cheong	Directly beneficially owned	Share options	3,000,000 share options	0.60%	(a)

Notes:

- (a) 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.

Save as disclosed herein, as at 31 October 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.

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

Name or category of participant	At 1.08.2005	Granted during the period	Exercised during the period	Lapsed during the period	Cancelled during the period	At 31.10.2005	Date of grant of share options (Note a)	Exercise period of share options	Exercise price of share options (Note b) HK\$
Directors									
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
	<u>6,200,000</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>6,200,000</u>			
Other employees	400,000	-	-	-	-	400,000	23.3.2001	10.10.2001 to 22.3.2011	0.55
	<u>6,600,000</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>6,600,000</u>			

Notes:

- The vesting period of the share options is from the date of the grant until the commencement of the exercise period.
- 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.

The exercise of the above 6,600,000 outstanding share options as at 31 October 2005, 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).

During the period ended 31 October 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 31 October 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 of shares/equity derivatives held	Percentage of the Company's issued share capital	Note
Concord Pharmaceutical Technology (Holdings) Limited ("CPT")	Corporation	Ordinary shares	400,000,000 shares	80%	a
Concord Business Management Limited ("CBM")	Through controlled corporation	Ordinary shares	400,000,000 shares	80%	a
Mr. Wong Sai Chung	Through controlled corporation	Ordinary shares	400,000,000 shares	80%	a

Notes:

- (c) CPT is a wholly-owned subsidiary of CBM. As at 31 October 2005, the entire issued share capital of CBM was owned by Mr. Wong Sai Chung. Accordingly, CBM and Mr. Wong Sai Chung is deemed to have interests in the 400,000,000 shares of the Company held by CPT.
- (d) 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 on 22 December 2004.

Save as disclosed above, as at 31 October 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 5.33 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 three months ended 31 October 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

Wong Sai Wa

Chairman

Hong Kong, 15 December 2005

As at the date of this announcement, 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. Garry Alides Willinge and Mr. Lai Chik Fan.