# Shandong Weigao Group Medical Polymer Company Limited*

(a joint stock limited company incorporated in the People's Republic of China with limited liability)

(Stock Code : 8199)






06 Annual Report

*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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*The directors (the "Directors") of Shandong Weigao Group Medical Polymer Company Limited (the "Company") collectively and individually accept full responsibility of this annual report. This annual report includes particulars given in compliance with the Rules Governing the Listing of Securities on GEM of the Stock Exchange (the "GEM Listing Rules") for the purpose of giving information with regard to the Company. The Directors, having made all reasonable enquiries, confirm that, to the best of their knowledge and belief: (i) the information contained in this annual 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 annual report misleading; and (iii) all opinions expressed in this annual 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

## DIRECTORS AND SUPERVISORS

*Executive Directors*

Mr. Zhang Hua Wei
Mr. Miao Yan Guo
Mr. Wang Yi
Mr. Wang Zhi Fan
Mr. Wu Chuan Ming

*Non-executive Directors*

Mr. Chen Xue Li
Mrs. Zhou Shu Hua

*Independent non-executive Directors*

Mr. Luan Jian Ping
Mr. Shi Huan
Mr. Lau Wai Kit
Mr. Li Jia Miao (appointed on 28 February 2007)

*Supervisors*

Ms. Bi Hong Mei
Mr. Miao Hai Sheng
Ms. Chen Xiao Yun

## CORPORATE INFORMATION

**Registered office and principal place of business in the People's Republic of China (the "PRC")**
312 Shi Chang Road
Weihai
Shandong Province
PRC

**Principal place of business in Hong Kong**
801, Chinachem Century Tower
178 Gloucester Road
Wanchai
Hong Kong

**Company secretary**
Ms. Wong Miu Ling, Phillis, ACIS

**Compliance officer**
Mr. Zhang Hua Wei

**Qualified accountant**
Ms. Chan Yuk Ying, Phyllis, CA

**Audit committee**
Mrs. Zhou Shu Hua
Mr. Luan Jian Ping
Mr. Shi Huan
Mr. Lau Wai Kit
Mr. Li Jia Miao (appointed as audit committee member on 14 March 2007)

# Corporate Information

**Authorised representatives**
Mr. Zhang Hua Wei
Ms. Wong Miu Ling, Phillis

**Auditors**
Deloitte Touche Tohmatsu
Certified Public Accountants

**Compliance adviser**
Goldbond Capital (Asia) Limited

**Hong Kong share registrars and transfer office**
Standard Registrars Limited

**Principal bankers**
1. Agriculture Bank of China, Weihai Branch
2. Bank of China, Weihai Branch

**Website of the Company**
www.weigaogroup.com

**Stock Code** 8199

# Corporate Profile

## Shandong Weigao Group Medical Polymer Company Limited

Shandong Weigao Group Medical Polymer Company Limited (the "Company") and its subsidiaries (together the "Group") is principally engaged in research, development, production and sale of medical device under the trademark of "Jierui" . The Company is recognised as an industrialization base to commercialise products developed by the State High-tech Research and Development (863) Program, the State High-tech Enterprise and the State Technology Center. The Group's main production facilities is situated in Weihai City in Shandong Province.

The Group is incorporated in the People's Republic of China. The Group has an extensive sales network comprising 17 sales offices, 21 customer liaison centers and over 100 municipal representative offices. It has an extensive customer base of 5,478 healthcare organizations and distributors, including 2,767 hospitals, 408 blood stations, 742 other medical units and 1,561 trading companies.

The Group produces a wide range of products of over 120 types with over 2,000 specifications, and they are grouped under six major categories, namely:-

I. Single use medical consumables and materials (including infusion (transfusion) sets, syringes, blood bags and blood component segregator consumable, blood sampling products, dental and anaesthetic consumables, medical PVC granules and non-PVC granules;

II. Orthopedic materials and instruments, including trauma products of steel plates and screws, spinal implants and artificial joints which are currently under development;

III. Medical needles which mainly include intravenous needles, syringe needles, intravenous catheter needles, blood sampling needles and irregular needles;

IV. Blood purification consumables, including puncture needles, blood tapping set, dialyzers and related consumables and immunoadsorption column for the treatment of immune system disorders such as systemic lupus erythematosus, organ transplant rejections and rheumatoid arthritis. Research and product registration are underway for adsorption columns for treatment of low density lipoprotein, endotoxin and hepatitis B;

V. Cardiovascular stent, mainly including drug eluting stent and balloon; and

VI. Pre-filled syringes for drug delivery.

The Group places strong emphasis on brand building and high quality products. The Group has established and maintained a quality system for the production of single-use sterile infusion sets, single-use sterile transfusion sets and single-use sterile syringes which meets the requirements of ISO9001:2000, ISO13485:1996 and obtained CDM certification awarded by China Quality Certification Centre for Medical Devices. The Group has implemented a quality assurance system for production of infusion sets, transfusion sets and single-use syringes which were accredited with EC Certification issued by TÜV Product Service Gmbh in December 1999 and were renewed in November 2003, November 2004, January 2005 and January 2006 respectively. On 5 December, 2003, the Group's product quality inspection center obtained an accreditation from China National Accreditation Board for Laboratories for the compliance with the State testing requirements and standards. On 23 June, 2005, the Group's trademark "Jierui" was recognised by the State Administration for Industry and Commerce as the Well-known Trademark in the medical device industry in the PRC. In September 2006, the single-use infusion (transfusion) medical device set under the trademark of "Jierui" was also accredited as "China Top Brand" by China Promotion Committee for Top Brand Strategy under General Administration of Quality Supervision, Inspection and Quarantine of the PRC.

The Group's products are mainly sold to PRC market. The Group is actively exploring business opportunities in the international markets, and its products have been exported to over 40 countries and regions, including the United States, Germany, Romania, Australia and the United Kingdom.

# Chairman's Statement

On behalf of the board of directors (the "Board") of Shandong Weigao Group Medical Polymer Company Limited (the "Company"), I would like to present the audited consolidated results of the Group for the year ended 31 December 2006. The Group's results in 2006 have continued to grow rapidly, with prominent effect from the adjustment to our operational structure and product mix, which laid down a foundation for our future development.

## FINANCIAL SUMMARY

During the year under review, the Group achieved record financial results in turnover and net profit attributable to shareholders.

As at 31 December 2006, the annual turnover amounted to RMB786,926,000, representing a growth of 38.1% over the previous year. Net profit attributable to shareholders was RMB170,921,000, representing a growth of 68.9% over the previous year. The significant growth in turnover and net profit attributable to shareholders have been mainly attributable to our market development strategy and effective adjustments made to our product mix. The successful strategy resulted the achievement of record high results with the development of high-end product market, expansion of markets to new customers and increase in sales to existing customers.

As at 31 December 2006, the total reserves of the Group amounted to approximately RMB602,184,000 (2005: RMB469,885,000).

## FINANCIAL HIGHLIGHT

| | **Audited** | | |
|---|---|---|---|
| | **2006** | 2005 | Growth % |
| | **RMB'000** | RMB'000 | |
| Turnover | **786,926** | 569,987 | 38.1% |
| Gross profit | **335,341** | 234,260 | 43.1% |
| Net profit attributable to shareholders | **170,921** | 101,200 | 68.9% |

## BUSINESS REVIEW

### Major developments

*(A) Successful achievement from international collaborations*

During the year under review, the Group has been focusing on international collaborations. The Group conducted in-depth discussions in various business sectors with a number of multi-national medical device companies. As at the date of this report, the Group has entered into loan agreement with International Finance Corporation ("IFC"), which has strengthened the financial capabilities and enhanced the brand awareness of the Company. The Group has entered into a legally binding letter of intent with Biosensors International Group Limited ("Biosensors International"), Biosensors International Pte Ltd. ("BSI"), a wholly owned subsidiary of Biosensors International, JW Medical Limited ("BVI Co")., Shandong JW Medical Systems Limited ("JW Medical") and Shandong Weigao Biosensors Medical Products Manufacturing Co., Limited ("Weigao Biosensors"), which has laid a solid foundation for the research and development capability on cardiovascular stent products of the Group and paving the way for expansion into international market. The Group has also entered into an initial letter of intent with Medtronic, Inc, a global leader in medical technology. These international collaborations will further strengthen the Group's business foundation and development capabilities, paving the way for the Group to become a leading medical device group in Asia by capitalizing on the advantages of the customer resources in the PRC market and the manufacturing capabilities of the Group.

*(B) Accreditation of "Jierui" trademark as "China Top Brand"*

In September 2006, the single-use infusion (transfusion) medical device set under the trademark of "Jierui" was also accredited as "China Top Brand" by China Promotion Committee for Top Brand Strategy under General Administration of Quality Supervision, Inspection and Quarantine of the PRC. The recognition was another significant accreditation obtained by the Group in addition to the "Well-known Trademark" which was the first and the only award accredited in the PRC medical device industry. The recognitions further enhanced brand awareness and competitiveness of the Group.

*(C) Improvement in internal control and corporate governance, enhancement in operation efficiency*

During the year under review, the Group implemented stringent budget management control on production cost and expenses, the application of enterprise resources planning system has increased the efficiency of production facilities and has enhanced the competitiveness of the Group by providing high quality products at competitive cost. With the improvement of the Group's supply chain system, the settlement methods, use of bulk purchase procurements, the bargaining power of the Group with the suppliers are strengthened, which helped to effectively control the working capital usage and to increase the profitability of the Group as a whole.

(D) *Adjustment in product mix and marketing strategies, seizing the high-end customers and high-end markets*

In 2006, the Group has been dedicated to and successfully implemented the strategic adjustments to its business mix and product mix, which captured on the business opportunities of the high speed growth driven by the demands for better quality and more advanced medical devices, and actively expanded its sales network. Sales of intravenous catheters, orthopedic products and cardiovascularstents made significant increase in profit contribution enabling the continued growth of business and enhancing shareholders' values.

For the year ended 31 December 2006, the Group has increased new customers of 98, including 38 hospitals and 8 blood stations. As at the date of this report, the total number of customers of the Group increased to 5,478, which includes 2,767 hospitals, 408 blood stations, 742 other medical institutions and 1,561 distributors.

(E) *Research and development and launch of new products*

During the year, the Group continued to increase its investments in research and development and established research and development centers with various research institutes, achieving remarkable results. The Group's WG-1 type non-PVC infusion set has been admitted as State Torch Plan Project, and the Group's Technology Centre has been jointly recognised as a National Enterprise Technology Centre by the National Development and Reform Commission, Ministry of Science and Technology, Ministry of Finance, the Customs and the State Tax Bureau, while preparation and application of the Group's new products such as medical light-proof plastic, thermal plastic elastic polyolefin (TPE) have been awarded with Technology Advancement Award by the government of the provincial and ministerial levels. For the year ended 31 December 2006, the Group obtained 25 new patents and is in the process of applying for another 28. New product registration certificates for 19 products have been obtained while 16 developed products are currently under the registration application process. Many of these products and technologies have attained international leading standards. The emphasis the Group placed on research and development helped to increase the Company's competitiveness, laying down a foundation for the Group to leverage on its customer base and to provide a new source of growth for the Group's profits.

During the year, the trauma and spinal products of Shandong Weigao Orthopedic Device Co., Ltd.（山東威高骨科材料有限公司）("Wego Ortho") have been launched, and achieved remarkable results. The cardiovascular stent of Shandong JW Medical Products Co., Ltd.（山東吉威醫療製品有限公司）("JW Medical"). 50% jointly owned company of the Group, has been successfully launched, and achieved great success. The introduction of intravenous catheter, orthopedic and stent signify the strategy of adjustment to the Group's business and product mix has been progressed to a new stage. It has also proven the Group's sales network and research and development capability. It has strengthened the Group's commitment to increase the business and product mix adjustments.

## FUTURE OUTLOOK

Year 2006 was an important year for the Group. The process of restructuring of the medical device industry in China will continue and will further intensify the market competition and affect the registration process of new products in the industry. Looking ahead, market integration will become a healthy development trend in the industry. Facing with intensifying market competition and pressure of rising operating costs, the Group will continue to maintain its growth momentum and profitability by adjusting its business and product mix, increasing research and development effort and expanding market share of its high-value added products. In addition, the Group will continue to launch new products to its extensive customer base through its expanding sales network. The Group will continue to adopt a China market orientated strategic plan to expand the domestic market.

Looking forward, the management anticipated that the competition in the market will intensify. With the introduction of new products and increase numbers of customers in the market, the Group will continue to implement the strategic adjustments to its business and product mix by capitalizing the Group's extensive sales network and cost advantages. The Group will continue to focus domestic market as its principal market and at the same time , the Group will continue to explore its overseas markets and strengthen its market position in the regional market in order to strive for competitiveness.

The Group will continue to adopt an open attitude to actively seek for joint venture opportunities with international market leaders. Leveraging the Group's advantages on sales network, quality and cost control capabilities, the Group will speed up the market share expansion in high value-added medical consumables in the industry and further expand its business to overseas markets and enhance its revenue growth.

The undersigned, together with the Board, are confident with the Group's future development. The Group will continue to strengthen its professional management team. With an indepth local knowledge and by applying advanced technology knowledge and innovative management skill, the Group and its employees are confident to meet new challenges.

## DIVDENDS

The Board of directors proposes a final dividend of RMB0.033 per share for the year ended 31 December 2006 in the forthcoming annual general meeting.

## CLOSURE OF REGISTER OF MEMBERS

The register of members in Hong Kong will be closed from Tuesday, 10 April 2007 to Wednesday, 9 May 2007, both dates inclusive, during which no transfer of shares of the Company will be registered. In order to qualify for attending the annual general meeting of the Company to be held on Wednesday, 9 May 2007, all transfers of shares of the Company accompanied by the relevant share certificates and transfer forms must be lodged with the Company's H Share Registrars, Standard Registrars Limited, at 26/F Tesbury Centre, 28 Queen's Road East, Hong Kong for registration no later than 4:00 p.m. on Wednesday, 4 April 2007.

## ACKNOWLEDGEMENTS

The Group's various achievements as mentioned above are attributable to the continued supports of the staff, customers and business partners and shareholders. I would like to take this opportunity to express my most sincere thanks for all your contributions!

**Chen Xue Li**
14 March 2007

# BUSINESS REVIEW

## MAJOR DEVELOPMENTS

The Group is dedicated to becoming a leading medical device supplier in Asia.

During the year, the Group achieved a significant progress in discussion regarding collaboration with international business players and financial institution. The Group has conducted in-depth discussions with a number of multi-national medical device companies in various business sectors.

(1) On 1 November 2006, a legally binding letter of intent ("LOI") has been entered into between the Group, Weigao Holding Limited ("Weigao Holding"), Biosensors International Group Limited ("Biosensors International"), Biosensors International Pte Ltd. ("BSI"), a wholly owned subsidiary of Biosensors International, JW Medical Limited ("BVI Co")., Shandong JW Medical Systems Limited ("JW Medical") and Shandong Weigao Biosensors Medical Products Manufacturing Co., Limited ("Weigao Biosensors"). Under the LOI, the Group intended to form a strategic alliance with Biosensors International, thereby enabling the reorganisation the shareholding structure of JW Medical, consolidation of product mix, thus strengthened the research and development capabilities and increased product reserves of JW Medical. It will help to explore the international market and further enhance the market share of JW Medical in the international cardiovascular stent market.

(2) On 2 March 2007, the Company entered into an eight years long term loan agreement for US$20 million with International Finance Corporation ("IFC"), a member of the World Bank Group. This cooperation can strengthen the Company's financing capability.

(3) On 11 March 2007, the Company has signed a non binding letter of intent with Medtronic, Inc. ("Medtronic") in relation to the proposed investment in the Company by Medtronic of up to a 15% of the enlarged issued share capital of the Company in the form of a combination of existing domestic shares and to be issued new H shares. In connection with the proposed investments, the parties intend to explore various business cooperation opportunities in manufacturing and distribution. Medtronic is the global leader in medical technology. Based on the framework set out in the letter of intent, both parties will pursue in-depth discussions and strive to reach a final cooperation.

These international collaborations will further expand the Group's business, strengthen research and development capabilities, leveraging our customer resources in the PRC market and manufacturing capabilities laying a strong foundation paving the way for the Group to be the leader in medical device industry in Asia.

During the year under review, the rapid growth and increase in profitability were mainly attributable to the Group's strategic adjustments to its business and product mix, improvement in operation efficiency and efforts in exploring new business, which mainly included sales of intravenous catheter, orthopedic products and drug eluting stents, which made significant increase in profit contribution enabling the continued growth of business and enhancing shareholders' values.

To enhance the operation efficiency, the Group implemented stringent budget management control on production cost and expenses, the application of enterprise resources planning system has increased the efficiency of production facilities and has enhanced the competitiveness of the Group by providing high quality products at competitive cost. With the improvement of the Group's supply chain system, the settlement methods, use of bulk purchase procurements, the bargaining power of the Group with the suppliers are strengthened, which helped to effectively control the working capital usage and to increase the profitability of the Group as a whole.

In September 2006, the Group's trademark of "Jierui" " " has been accredited as "China Top Brand" product by China Promotion for Top Brand Strategy Committee under General Administration of Quality Supervision, Inspection and Quarantine of the PRC, which was another significant accreditation obtained by the Group's products in addition to the only "Well-known Trademark" accredited in the medical device industry in the PRC. It further enhanced brand awareness and competitiveness of the Group.

## STRATEGIC ADJUSTMENTS TO BUSINESS AND PRODUCT MIX

In respect of strategic adjustments to product composition, the Group focused on researching in high-technology and high value-added products, and increasing in the marketing and sales effort on high value-added products such as intravenous catheters, high-end infusion sets, CT developer syringes and safety auto-disable syringes, resulting a further increase in contribution of high value-added products to the Group's revenue.

During the period under review, the Group has been dedicated to and successfully implemented the strategic adjustments to its business mix, the increase in capital expenditures focus the development on orthopedic, blood purification and drug eluting stent products.

(1) Shandong Weigao Orthopedic Device Co., Ltd ("Wego Ortho"), a subsidiary of the Company, is principally engaged in the research and development, production and sales of technologically advanced and high value-added products such as medulla nail series, steel plate series and bone connecting screw series and spine fixing series. During the year under review, the product series of trauma and spine have been launched with remarkable results. The product quality has been well recognised by the market, rapidly penetrating the market and driving sales growth. For the twelve months ended 31 December 2006, Wego Ortho recorded a turnover of approximately RMB67,502,000, contributing to the continuous growth in turnover and profit of the Group.

(2) 山西威高華鼎醫療器械製造有限公司 (Shanxi Weigao Huading Medical Equipment Manufacturing Company Limited) ("Weigao Huading"), a company established by 威海威高血液淨化製品有限公司 (Weihai Weigao Blood Purified Product Co., Ltd.) ("Weigao Blood") and an independent third party, has obtained registration and commenced sales of its products during the year. Weigao Blood is in the process of obtaining the production registration for its plasma segregator, lavage set and recombinant protein adsorption column. The development of sales and distribution network is well underway and the trial operation of the production facilities was completed.

(3) Production and sales of drug eluting stent by JW Medical, which is 50% held by the Company, recorded significant growth during the year. Its sales network in the PRC has been rapidly expanded, and its development of international market has been well underway. JW Medical has become a significant source of profit to the Group. JW Medical will continue to leverage on its technology and cost advantages and to increase its efforts in promoting its products to domestic and international markets, enhancing the competitiveness of the Group in the high-end market.

The introduction of intravenous catheter, orthopedic and stent signify the strategy of adjustment to the Group's business and product mix has been progress to a new stage. It has also proven the Group's sales network and research and development capability. It has strengthened the Group's commitment to increase the business and product mix adjustments.

For the year ended 31 December 2006, the total investments of the Group in fixed assets amounted to approximately RMB162,856,000 (including RMB45,000,000 being the deposit for acquisition of property). The capital expenditure on increasing production capacity and the new projects will significantly enhance the competitiveness of the Group and speeded up the pace in the adjustment to the business and product mix. With diversified product types and product range, the Group enjoys competitive advantage in expanding its customer base.

## RESEARCH AND DEVELOPMENT

During the year under review, the Group continued to increase its resource on research and development. In addition to in-house research and development capability, the Group also established alliances with two research institutes of the China Academy of Sciences (Changchun Applied Chemistry Research Institute and Dalian Chemistry-Physics Research Institute) and a number of top medical educational institutions in the PRC, such as Beijing 301 Hospital, the First Subordinate Hospital of the Third Military Medical University in the areas of production, research and academic exchange. The Group expanded its research team with post-doctorate researchers and has successfully achieved remarkable results in research and development.

For the year ended 31 December 2006, 25 new patents were registered by the Group and certificates of 19 new products were obtained. The applications for registration of patent for 28 new products are in progress while application for registration for 16 newly developed products are underway. By placing strong emphasis on research and development, it enhances the Group's competitiveness and allows the Group to leverage on its customer base and to provide the Group with new growth drivers.

(1) The WG-1 type non-PVC infusion set (超低密度聚乙烯輸液器 ultra density polypropylene infusion set) developed by the Company with proprietary intellectual property right has been admitted in the "2006 State Torch Plan — Hi-tech Industry Model Project" by the Ministry of Science and Technology. The primary components of ultra density polypropylene infusion set are high elastic polyolefin and transparent granules. The development of high quality products serves as import replacement.

(2) The Technology Centre of the Group has been jointly recognised as a National Enterprise Technology Centre for medical device industry by the National Development and Reform Commission, Ministry of Science and Technology, Ministry of Finance, the Customs and the State Tax Bureau. The focus of Weigao Technology Centre will be on biological protein and biological medical material, and the development of treatment for contagious disease and development of medical devices in the treatment of major diseases, and development of biological medical materials for replacement of human organs and degradable medical materials, develop high-end medical devices and to strengthen the core competitiveness of the Group.

(3) The successful development of medical light-proof plastic, production and application of thermal plastic elastic polyolefin (TPE), and the successful development of new products such as fiber plasma segregator, single-use clipping self-destructive syringe and single-use test-tube sampling blood bag by the Group have been awarded with Technology Advancement Awards by the government of provincial and ministerial levels. It is expected there will be wide applications for these products.

During the year under review, the total research and development expenses amounted to approximately RMB12,541,000 (2005: RMB10,536,000) (including capitalised research and development expenditure of RMB3,669,000 (2005: RMB2,202,000)), representing 1.6% of the consolidated total turnover of the Group.

## NEWLY ADDED PRODUCTION CAPACITY

The Group's newly invested syringe production workshop, with a self-developed semi-automated production line, covering an area of approximately 2,400 square meters commenced operation in February 2006. The annual production capacity of the new production facilities is approximately 300 million units of single-use sterile syringes.

In order to integrate the upstream and downstream resources of needles production, to further the vertically integrated production process, and to minimize the purchasing cost of raw tube of precision needle required for production of needles, Jierui Subsidiary invested a total of approximately RMB18,500,000 to purchase the production equipment of needle raw tubes and a production plant covering an area of approximately 1,000 square meters. The expected production capacity is approximately 300 tonnes of needle raw tubes.

During the year under review, production volume of the Group's products as compared with that in the previous year is as follows:

(1) approximately 219,361,000 sets of single-use sterile infusion (transfusion) sets, increased by 4.9%;

(2) approximately 363,580,000 sets of single-use sterile syringes, increased by 17.0%;

(3) approximately 11,761,000 sets of single-use sterile blood transfusion consumables (including blood bag products), increased by 12.6%;

(4) approximately 2,108,000 sets of single-use sterile dental and anesthetic products, increased by 15.8%;

(5) approximately 77,091,000 sets of blood sampling products, increased by 117.3%;

(6) approximately 1,284,481,000 sets of medical needle products, increased by 30.8%;

(7) approximately 9,730 tonnes of PVC granules, increased by 2.7%;

(8) approximately 1,187,000 pieces (sets) of orthopedic materials;

(9) approximately 89,453,000 sets (pieces) of other products, increased by 83.2%.

With the enterprise resources planning system ("ERP") implemented since 2005, the Group has strengthened its management on production planning. It has been more effective in controlling production output and reducing working capital tied up in consumable materials.

At the same time, the Group increased the proportion of producing high value-added products, and decreased the production of low value-added and low return products. The strategy has raised profit contribution from individual items and ultimately increased the Group's overall profitability.

## SALES AND MARKETING

The integration of the Group's sales channel and adjustment in business and product mix has been very effective.

During the year under review, the Group strengthened its management on sales system, integrated sales channels and maximized return particularly on high return client in order to increase the contribution rates of individual customers. It has transferred certain customers with high maintenance cost to be covered by distributors. It resulted an increase in the average revenue per customer by 36.0% as compared with that of the previous year.

In 2006, the Group has increased the number of customers by 98 (including approximately 38 hospitals and 8 blood stations). As at the date of this report, the Group has a customer base of 5,478 (including 2,767 hospitals, 408 blood stations, 742 other medical units and 1,561 trading companies).

Comparison of the sales of various products by geographical district with that of the previous year is set out as follows:

## REVENUE BY GEOGRAPHICAL SEGMENTS

**For the twelve months ended 31 December**

| Region | **2006** | | 2005 | | Growth |
|---|---|---|---|---|---|
| | **RMB'000** | **%** | RMB'000 | % | % |
| Northeast | **139,743** | **17.8** | 118,833 | 20.9 | 17.6 |
| Northern | **186,538** | **23.6** | 144,162 | 25.3 | 29.4 |
| Eastern and Central | **267,292** | **34.0** | 147,085 | 25.8 | 81.7 |
| Southwest | **43,948** | **5.6** | 30,385 | 5.3 | 44.6 |
| Northwest | **30,841** | **3.9** | 20,292 | 3.6 | 52.0 |
| Southern | **81,880** | **10.4** | 73,640 | 12.9 | 11.2 |
| Overseas | **36,684** | **4.7** | 35,590 | 6.2 | 3.1 |
| Total | **786,926** | **100.0** | 569,987 | 100.0 | 38.1 |

Adjustment to its business and product mix is another important factor contributing to the increase in the Group's results during the year. During the year under review, the Group increased its sale and marketing effort on high value-added products such as orthopedic products, drug-eluting stents, intravenous catheter, CT developer syringes and pain killing pumps. It resulted in an increase in the proportion of sales generated from high value-added products. The consolidated gross margin has been increased by 1.5% to 42.6% as compared with that of last year. Comparison of the growth of sales of the principal products with that in last year is set out as follows:

## REVENUE BY PRODUCTS

| | | For the twelve months ended 31 December | | |
|---|---|---|---|---|
| | | **2006** | 2005 | Growth |
| | **Product category** | **RMB'000** | RMB'000 | % |
| *Self-produced products* | Self-produced products Consumables | | | |
| | Infusion sets | **216,394** | 187,739 | 15.3 |
| | Syringes | **175,411** | 156,839 | 11.8 |
| | Blood bags | **83,499** | 73,589 | 13.5 |
| | Dental and anesthetic consumables | **11,082** | 9,913 | 11.8 |
| | Blood sampling products | **20,078** | 10,233 | 96.2 |
| | Medical needles | **54,906** | 17,959 | 205.7 |
| | Other consumables | **58,089** | 29,382 | 97.7 |
| **Sub-total for consumables** | | **619,459** | 485,654 | 27.6 |
| | Orthopedic products | **67,502** | 1,074 | 6,185.1 |
| | Blood purification consumables | **8,598** | 2,859 | 200.7 |
| | PVC granules | **56,204** | 49,558 | 13.4 |
| *Trading products* | Medical instruments | **33,279** | 29,618 | 12.4 |
| | Other products | **1,884** | 1,224 | 53.9 |
| **Total** | | **786,926** | 569,987 | 38.1 |

## HUMAN RESOURCES

As at 31 December 2006, the Company employed a total of 5,456 employees. Comparisons of the headcount by departments over last year are as follows:

| Departments | 2006 | 2005 |
|---|---|---|
| Research and development | 144 | 141 |
| Sales and marketing | 656 | 636 |
| Production | 4,307 | 4,390 |
| Purchasing | 28 | 29 |
| Quality control | 85 | 80 |
| Management | 55 | 54 |
| Finance and administration | 181 | 178 |
| Total | 5,456 | 5,508 |

With the technical enhancement in the Group's production plants and the increase in the level of production automation, the number of the production workers decreased by approximately 2% as compared to 2005. The Group strengthened its research and development, and marketing, and thus, there was an increase in the number of staff in these departments.

All employees of the Group reside in the PRC except for the qualified accountant and company secretary who reside in Hong Kong. During the year, total cost incurred by the Group in relation to staff salaries, welfare and social insurance amounted to RMB94,356,000 (2005: RMB73,433,000).

## REMUNERATION SYSTEM

The Group's remuneration policy has been determined based on its performance, changes in the local consumption level and the competition in the human resources market. The remuneration policy so determined has become the principles of the salary levels of employees recruited for different positions. The salary of each employee is determined according to the employee's performance, ability, employment conditions and the salary standards set by the Company. Remuneration of Directors is determined by the Remuneration Committee with reference to operation results of the Company, personal performance and market competitions.

# FINANCIAL REVIEW

During the year under review, the Group recorded significant growth in both turnover and net profit attributable to shareholders.

For the year ended 31 December 2006, the annual turnover amounted to RMB786,926,000, representing an increase of 38.1% over the previous financial year. Net profit attributable to shareholders amounted to RMB170,921,000, representing an increase of 68.9% over the previous financial year. The significant growth in turnover and net profit was mainly attributable to change in product mix, increase in efficiency and effective market development.

## FINANCIAL SUMMARY

| | **2006**<br>**RMB'000**<br>**Audited** | 2005<br>RMB'000<br>Audited | Growth% |
|---|---|---|---|
| Turnover | **786,926** | 569,987 | 38.1 |
| Gross profit | **335,341** | 234,260 | 43.1 |
| Profit before interests, taxation, depreciation and amortization | **254,175** | 143,481 | 77.1 |
| Net profit attributable to shareholders | **170,921** | 101,200 | 68.9 |

# LIQUIDITY AND FINANCIAL RESOURCES

During the year, the Group maintained a sound financial condition. As at 31 December 2006, the Group has a cash and bank balance of approximately RMB115,131,000. For the year ended 31 December 2006, the Group maintained healthy cash flow with net cash generated from operating activities amounted to approximately RMB176,547,000.

During the year under review, the Group obtained bank loans of RMB432,043,000 and repaid bank loans of RMB433,200,000. Short-term loans reduced by RMB72,157,000, while long-term loans increased by RMB71,000,000. As at 31 December 2006, the bank and other borrowings of the Group repayable within one year amounted to RMB105,043,000 (2005: RMB177,200,000), and bank and other borrowings repayable after one year amounted to RMB281,000,000 (2005: RMB210,000,000).

In 2006, the total interest expenses of the Group amounted to approximately RMB21,519,000 (2005: RMB17,038,000).

## GEARING RATIO

As at 31 December 2006, the gearing ratio of the Group, being the ratio of total borrowings net of cash and bank balances to total equity attributable to shareholders, was 0.39 (2005: 0.41). The decrease in gearing ratio was mainly due to the increase in reserves in the year.

## FOREIGN EXCHANGE RISKS

The Group's purchases and sales are mainly conducted in the PRC. During the year under review, the Group has not encountered with any material difficulty due to fluctuations in exchange rates nor has its operating funds been affected.

## CONTINGENT LIABILITIES

The Group did not have any material contingent liabilities as at 31 December 2006.

## MATERIAL SUBSIDIARY INVESTMENTS/FUTURE MATERIAL INVESTMENTS

On 4 August 2006, the Company acquired 39% interest in Shenyang Weigao Jinbao Trading Co., Ltd. (瀋陽威高金寶商貿有限公司) ("Weigao Jinbao") (the Company's subsidiary) from Ren Fei, a former substantial shareholder and other shareholders of Weigao Jinbao, at a consideration of approximately RMB3,099,000. Upon completion of the transaction, the interest in Weigao Jinbao held by the Company increased from 51% to 90%.

In order to integrate the upstream and downstream resources of needles production, to further vertically integrated the production process, and to minimize the purchasing cost of raw tube of precision needle required for production of needles, the Jierui Subsidiary invested a total of approximately RMB18,500,000 to purchase the production equipment of needle raw tubes and a production plant covering an area of approximately 1,000 square meters. The expected production capacity is approximately 300 tonnes of needle raw tubes.

In order to meet the increasing demand for its drug eluting stents, JW Medical, a 50% jointly owned company of the Group invested in a new production base and to expand the existing production capacity. As at the date of this report, JW Medical invested a total of approximately RMB24,893,000.

The spinal products and trauma products launched by Wego Ortho early this year have been well received by the market. Wego Ortho is one of the few domestic manufactures which is able to produce spinal products and market under its own brand. In order to expand the market share of orthopedic products, the Group decided to invest up to RMB73,000,000 to acquire a premises from 威海慧豐醫用材料有限公司, an independent third party, as the production base of orthopedic products. As at the date of this report, the Group has paid approximately RMB45,000,000 for the acquisition.

As at 31 December 2006, the Group has no material capital commitments other than the above planned investments, nor any future plans to participate in any material investment or to acquire any capital assets, and no material acquisition and disposal of any other subsidiaries and associated companies have been conducted during the period.

## CAPITAL COMMITMENTS

As at 31 December 2006, the Group and the Company had commitments for acquisition of property, plant and equipment which were contracted but not provided in the financial statements amounted to RMB31,578,000 (2005: RMB18,189,000). These commitments are expected to be satisfied by the internal funding of the Group.

### PLEDGE OF THE GROUP'S ASSETS

As at 31 December 2006, the Group had pledged land use rights and buildings with a net book value of approximately RMB237,402,000 (2005: RMB157,131,000) and pledge bank deposits of RMB 22,328,000 (2005: RMB22,657,000) to secure bills and banking facilities of the Group.

## RESERVES AND DISTRIBUTABLE RESERVES

As at 31 December 2006, the total reserves of the Group amounted to RMB602,184,000 (2005: RMB469,885,000).

Under the PRC laws and regulations, the Company's distributable reserves will be based on the lower of the amount calculated according to the PRC accounting principles and rules and the amount calculated according to the Hong Kong generally accepted accounting principles. As at 31 December 2006, the distributable reserves of the Company were RMB108,287,000 (2005: RMB101,201,000).

## FUTURE OUTLOOK

Looking forward, the Directors anticipated that market demands for single-use medical devices in the PRC will maintain to grow rapidly. At the same time, the Directors anticipate that process of restructuring of the medical device industry in the PRC will continue and intensify, in the short term, it will delay in the settlement of accounts receivables and tie up an increased amount of working capital. However, in the long term, it will be beneficial for the development of the medical device market, and will allow the Group to fully leverage its advantage with the direct sales network.

Facing with the intensifying market competition and pressure of rising operation costs, the Group will focus its operation strategies on the following:

1. Speeding up business mix adjustment, maintaining and strengthening its position in medical device market, speeding up development of new business, through various channels exploring collaboration opportunities with world leading medical device companies.

2. Increasing in resource allocation on changing the product mix, focusing on developing the market of high value-added products, in particular, intravenous catheter needles, drug eluting stents, orthopedic products, CT developer sterile syringe, and increasing the rate of contribution of each product type to the Group's profit.

3. Strengthening on market strategies to continue adjusting the sales channel, gradually shifting direct sales to customers with low return and high maintenance cost over to be covered by distributors, and gradually promoting direct sales of drug eluting stents and orthopedic products to high-end customers.

4. Strengthening on management of market resources, developing new customers and strengthening the relationship with existing customers, increasing marketing activities, expanding sales team and developing a strong sales network leading to continuous sales growth.

5. Improving management process and strengthening budget management control and the Manufacturing Resources Planning II to better manage cost control and production, lesser the impact of increase in material costs.

The Group is confident with the future development. The Group will continue to strengthen its professional management team. With an indepth local knowledge and by applying advanced technology knowledge and innovative management skill, the Group and its employees are confident to meet new challenges.

## COMPARISON OF THE BUSINESS OBJECTIVES WITH THE ACTUAL BUSINESS PROGRESS

| Statements of business objectives as set out in the prospectus for the placing in 2004 (the "2004 Placing") (Please refer to the "Explanations to the use of proceeds" for details) | Actual business progress from the beginning of the year to 31 December 2006 |
|---|---|

## RESEARCH AND DEVELOPMENT

| | |
|---|---|
| To invest RMB1,000,000 in the research and development of new products | The Group has obtained 25 new patents and 19 new product certificates, and 28 new products are in progress while application for registration for 16 newly developed products are underway. Total expenses on research and development amounted to RMB12,541,000, of which RMB1,000,000 was from the proceeds of the 2004 Placing. |

## BREAKDOWN ON THE USE OF PROCEEDS

**Project**

| | |
|---|---|
| 1. To apply approximately RMB34,800,000 of the proceeds from the 2005 Placing for the purchase of machinery and equipment for Wego Ortho | Actual invested amount as at 31 December 2006 was approximately RMB34,800,000, of which approximately RMB13,200,000 was invested in 2005, and approximately RMB21,600,000 was invested in 2006 |
| 2. To apply approximately RMB24,880,000 of the proceeds from the 2005 Placing for the purchase of machinery and equipment for Weigao Blood | Actual aggregate invested amount as at 31 December 2006 was approximately RMB24,880,000, of which approximately RMB10,500,000 was invested in 2005, and approximately RMB14,380,000 was invested in 2006 |

| | Planned<br>*RMB'000* | 2006 Actual<br>*RMB'000* |
|---|---|---|
| 2005 Placing | | |
| Orthopedic materials | 34,800 | 21,600 |
| Blood purification | 24,880 | 14,380 |
| Total | 59,680 | 35,980 |

# Report of The Supervisory Committee

To all shareholders:

For the year ended 31st December, 2006, the entire members of the Supervisory Committee of the Company have complied with the Company Law of the PRC, the relevant regulations of Hong Kong and the Articles of Association of the Company (the "Relevant Regulations"), and under the principles of fidelity, have diligently and seriously discharged their duties to safeguard the benefits of the Company's shareholders and the Company.

During the year, the Supervisory Committee has provided reasonable opinions and recommendations to the Board over the business and development plans, and has performed serious and effective supervision on the Company's policies on whether they were in compliance with the Relevant Regulations and whether the interests of the Company shareholders have been protected.

The Supervisory Committee, having made inspections, considers that the audited financial report of the Company truly and fairly reflected the Company's operating results and assets situation for the year. The Supervisory Committee considers that the Report of the Board and the profits distribution plan proposal are in compliance with the Relevant Regulations. The Supervisory Committee has attended the Board meetings. The Supervisory Committee considers that the meetings were convened in compliance with the Relevant Regulations. The Supervisory Committee considers that the Company's Board members, general manager and other senior management have strictly abode with the principles of fidelity, hard working, and conscientiously performing their duties for the best benefits of the Company. None of the Directors, general manager and other senior management of the Company has been found to have abused their duties, harmed the Company's benefits or infringed the interests of the Company's shareholders and staff, and made violation of the Relevant Regulations.

The Supervisory Committee is satisfactory with the various works of the Company and the operating results obtained, and is fully confident on the future development prospects of the Company.

By Order of the Supervisory Committee
**Shandong Weigao Group Medical Polymer Company Limited**
**Bi Hong Mei**
*Chairman*

Weihai, Shandong Province, the PRC
14 March 2007

## Corporate Governance Practices

The Board of Directors of the Company believes that corporate governance is essential to the success of the Company and has adopted various measures to ensure its strict compliance with relevant regulatory requirements, a high level of transparency in corporate governance and an excellent performance in operation.

The Company has complied with all of the code provisions of the Code on Corporate Governance Practices (the "Code") as set out in Appendix 15 of the Rules Governing the Listing of Securities on The Growth Enterprise Market of The Stock Exchange of Hong Kong Limited.

The following summarizes the corporate governance practices of the Company:

## A. Directors

### Board of Directors

The Board meets at least quarterly. Regular meetings are convened once every three months. Directors can attend meetings in person or by means of electronic communication. Set out below is the number of Board meetings of the Company convened in year 2006 and the individual attendance of each Director:

Number of Board meetings held during the year 2006: 11

Details of individual attendance of each Director:

| | **Attendance in 2006 (%)** |
|---|---|
| Executive Directors | |
| Mr. Zhang Hua Wei | 91% |
| Mr. Wang Yi | 73% |
| Mr. Miao Yan Guo | 82% |
| Mr. Wang Zhi Fan | 64% |
| Mr. Wu Chuan Ming | 91% |
| Non-executive Directors | |
| Mr. Chen Xue Li | 91% |
| Mrs. Zhou Shu Hua | 73% |
| Independent non-executive Directors | |
| Mr. Shi Huan | 100% |
| Mr. Luan Jian Ping | 100% |
| Mr. Lau Wai Kit | 64% |
| Mr. Li Jia Miao (appointed on 28 February 2007) | 0% |

Notices of all regular Board meetings are issued 14 days before the meetings.

Minutes of Board/ committee meetings are recorded, and draft minutes and final version are submitted to Directors for review within reasonable time after the meetings, normally 14 days after the meetings.

Secretary of the Board assists the chairman to establish meeting agenda, and each Director may request inclusion of items in the agenda.

Matters on transactions where Directors are considered having conflict of interests or material interests will not be dealt with by way of written resolutions. The Directors concerned can express views but will not be counted in the quorum of meetings and shall abstain from voting on the relevant resolution(s).

All Directors have access to the company secretary who is responsible for ensuring that the Board procedures are complied with, and advising the Board on compliance matters.

Minutes of Board/committee meetings are kept by the company secretary and are open for inspection by Directors.

### Chairman and chief executive officer

Mr. Chen Xue Li, a non-executive Director, is the chairman of the Board, and Mr. Zhang Hua Wei, an executive Director, is the chief executive officer of the Company.

The chairman of the Board is appointed by the Board itself, who is responsible for the leadership of effective operation of the Board, and ensuring that all major and appropriate issues are discussed by the Board on a timely basis and in a constructive manner.

The chief executive officer is appointed by the Board. He is responsible for the management of daily operations of the Company and the implementation of the strategies and plans determined by the Board.

### Composition of the Board

The Board comprises 11 Directors, of which four are independent non-executive Directors, two are non-executive Directors and five are executive Directors. On 28 February 2007. Mr. Li Jia Miao was appointed as independent non-executive Director. The Directors are:

| | |
|---|---|
| Independent non-executive Directors: | Mr. Shi Huan, Mr. Luan Jian Ping, Mr. Lau Wai Kit and Mr. Li Jia Miao* |
| Non-executive Directors: | Mr. Chen Xue Li and Mrs. Zhou Shu Hua |
| Executive Directors: | Mr. Zhang Hua Wei, Mr. Wang Yi, Mr. Miao Yan Guo, Mr. Wang Zhi Fan and Mr. Wu Chuan Ming |

The independent non-executive Directors are explicitly identified in all corporate communications.

*Note: Mr Li Jia Miao was appointed as independent non-executive director and a member in audit committee on 28 Feburary 2007 and 14 March 2007 respectively.

## Experience

The executive Directors and non-executive Directors possess administrative leadership, diversified knowledge and extensive management experience in the industry. The independent non-executive Directors possess extensive knowledge, experience and judgements in different areas. Among them, Mr. Lau Wai Kit possesses extensive working experience in finance and accounting. The Board will seriously consider the objective views of the independent non-executive Directors for making decisions, and regard this as an effective guidance for the Group's business direction.

## Nomination, Appointment and removal of Directors

All of the non-executive Directors of the Company are appointed for a specific term of three years.

The Company has not experienced any casual vacancy for members of the Board. In the event that there is such circumstance, the Director appointed to fill a casual vacancy should be subject to election by shareholders at the first general meeting after his appointment.

Each Director shall be subject to retirement by rotation at least once every three years.

The Board selects and nominates Director candidates based on whether they possess the skills and experience needed for the Group's development.

The Company has not set up a nomination committee, the Board as a whole is responsible for reviewing the Board composition, developing and formulating the relevant procedures for nomination and appointment of directors, monitoring the nomination of directors and assessing the independence of independent non-executive directors of the Company.

## Directors' responsibility

The Board manages the business of the Company on behalf of its shareholders. The Directors consider that they are obliged to fulfill their responsibilities in a prudent, diligent and faithful manner, so as to create value for shareholders and safeguard the best interests of the Company and its shareholders.

The Company has adopted a code of conduct regarding transactions in securities by directors on no less exacting terms than the required standard of dealings set out in Rules 5.48 to 5.67 of the GEM Listing Rules. Specific enquiries have been made with all Directors of the Company and they have confirmed that they have fully complied with the required standard of dealings and the code of conduct of the Company regarding securities transactions throughout the year 2006.

## B. Remuneration of Directors and Senior Management

### Remuneration Committee

The Company established a remuneration committee on 12 August 2005 in accordance with the requirement of the Code. The remuneration committee comprises four independent non-executive Directors, namely Mr. Shi Huan, Mr. Luan Jian Ping, Mr. Lau Wai Kit and Mr. Li Jia Miao who was appointed as committee member on 14 March 2007. The chairman of the remuneration committee is Mr. Shi Huan;

The remuneration committee has reviewed the remuneration policy, the performance and the remuneration of executive Directors and members of senior management, the existing terms of service contracts of the executive Directors. The objective of the remuneration policy is to ensure that the Company is able to attract, retain and motivate high-caliber staff, which is vital to the success of the Company.

In reviewing and determing the remuneration packages of the executive Directors and members of senior management, the remuneration committee considers their responsibilities, skills, expertise and contribution to the Group's performance and whether remuneration packages are competitive and sufficient to ensure that the Group is able to attract and retain the best available executive talent.

No Director or executive officer can determine his/her own remuneration. The remuneration of all Directors is subject to approval at shareholders' meetings.

During the year, one meeting has been held by the remuneration committee. All members of the remuneration committee attended the meeting during which the responsibilities of the remuneration committee were defined and matters such as the remuneration policy, incentive mechanism of the Directors and senior management of the Group were reviewed. The chairman of the remuneration committee reports the findings and provides recommendations to the Board after each meeting.

The scope of responsibilities of the remuneration committee is available for inspection upon request.

## C. Accountability and Audit

### Financial Reporting

All Directors are provided with explanations and information by the management of the Company so as to enable them to have discussions and make assessment at Board meetings.

All Directors acknowledge the responsibility for the preparation of its accounts, with the responsibility statement in respect to the financial reports made by the Directors set out in this annual report. The auditors have also made a statement about their responsibilities in the auditor's report.

The Board presents a comprehensive, balanced and understandable assessment on the position and prospects of the Group in all shareholder communications.

### Internal control

Directors are responsible for reviewing the internal control and risk management system of the Company periodically to ensure its effectiveness and efficiency. With the support of the internal audit department, they will review the practices, procedures, expenditure and internal control of the Company and its subsidiaries on a regular basis. The management will regularly monitor the concerns as reported by the internal audit department to ensure appropriate remedial measures have been implemented. The Board or senior management can also request the internal audit group to review the specific scope of concerns and report the significant findings of such review to the Board and the audit committee.

The Board has conducted a review of the effectiveness of the system of internal control of the Group.

### Audit committee

The audit committee of the Company comprises independent non-executive Directors, namely Mr. Lau Wai Kit, Mr. Shi Huan, Mr. Luan Jian Ping and Mr. Li Jia Miao (appointed on 14 March 2007) and a non-executive Director, Mrs. Zhou Shu Hua. The chairman is Mr. Lau Wai Kit.

The terms of reference of the audit committee have been clearly defined. Its principal responsibilities include:

- To serve as a focal point for communication amongst Directors and auditors in respect of the duties relating to financial and other reporting, internal control, external and internal auditors and such other matters as the Board determines from time to time.

- To assist the Board in fulfilling its responsibilities by providing independent reviews and supervising financial reporting, by satisfying themselves as to the effectiveness of the internal control of the Group and the adequacy of the external and internal audits.

➢ To review the scope and findings of internal audit procedures, to ensure coordination between internal and external auditors, and to ensure that the preparation of the financial reportings complied with the applicable accounting standards and requirements.

➢ To review the appointment of the external auditors on an annual basis, including a review on the scope of audit and approval of audit fees.

➢ To review annual, quarterly and interim financial statements prior to their approval by the Board, and to recommend application of accounting policies and changes to financial reporting requirements.

➢ To ensure the objectivity and independence of succession auditors.

During the year of 2006, the audit committee has convened four meetings, at which, they have primarily discussed and reviewed the quarterly, interim and annual results and have discussed and considered the internal control procedures of the Group. The attendance of each Director is set out below:

| | **Attendance in 2006 (%)** |
|---|---|
| Independent non-executive Directors | |
| Mr. Lau Wai Kit | 100% |
| Mr. Shi Huan | 100% |
| Mr. Luan Jian Ping | 100% |
| Mr. Li Jia Miao (appointed as audit committee member on 14 March 2007) | — |
| Non-executive Director | |
| Mrs. Zhou Shu Hua | 100% |

The scope of responsibilities of the audit committee is available for inspection upon request.

There was no disagreement between the audit committee and the Board in respect of the selection, appointment, resignation or removal of external auditors during the year of 2006.

The audit committee can consult independent professional advice in accordance with stated procedures at the expense of the Company.

In 2006, the audit fees paid to the external auditors by the Company was approximately RMB2,136,000, of which: approximately RMB863,000 represented the audit fees incurred for the audit of the financial results of the Group for the year 2006 and approximately RMB1,273,000 were related to audit fees incurred for the proposed application of the Listing of the H Shares of the Company on the Main Board of the Stock Exchange in Hong Kong.

## D. Mandate Granted to the Board

The Board should assume the responsibility for the leadership and monitoring of the Company, and is collectively responsible for promoting the success of the Company. The responsibilities of the Board are defined explicitly in the articles of association of the Company.

(1) to be responsible for convening shareholders' meetings and report on its work at shareholders' meetings;

(2) to implement the resolutions passed at shareholders' meetings;

(3) to determine the business plans and investment plans of the Company;

(4) to formulate the annual fiscal budgets and final accounts of the Company;

(5) to formulate profit distribution proposals and loss recovery proposals of the Company;

(6) to formulate proposals for increasing or reducing of the registered capital of the Company and proposals for issue of debentures of the Company;

(7) to draft proposals for the merger, division and dissolution of the Company;

(8) to determine the establishment of the internal management bodies of the Company;

(9) to appoint or dismiss the general manager of the Company, and to appoint or dismiss the deputy general manager and other senior management, including the person in charge of finance, pursuant to the recommendations of the general manager, as well as to determine their compensations;

(10) to formulate the basic management system of the Company;

(11) to formulate proposals for amendments to the articles of association of the Company; and

(12) to exercise other functions as stipulated by the articles of association or granted by the shareholders' meetings.

The Board has granted authority to the chief executive officer to implement the following strategies and to be responsible for the day-to-day operation:

(1) to be in charge of the management of production and operation and to organize the implementation of the resolutions of the Board;

(2) to organize the implementation of the annual business plans and investment plans of the Company;

(3) to draft proposals for the establishment of internal management bodies of the Company;

(4) to draft the basis management system of the Company;

(5) to formulate the basic rules and regulations of the Company;

(6) to propose the appointment or removal of the deputy general manager and other senior management, including the person in charge of finance, of the Company;

(7) to appoint or dismiss the management personnel other than those required to be appointed or dismissed by the Board; and

(8) to exercise other functions granted by the articles of association and the Board.

The chief executive officer grants authorisation to chief financial officers, and senior management within his terms of reference.

The Board is supported by two committees, namely the audit committee and the remuneration committee. Each of the committees has its defined terms of reference covering its duties, rights and functions. The chairmen of the respective committees report to the Board regularly and make recommendations on matters discussed as appropriate.

## E. Communications with shareholders

Separate resolutions are proposed at general meetings on each substantially separate issue, including the election of individual Directors.

The shareholders' meeting provides an effective forum for shareholders to exchange views with the Board. The chairman, together with the chairmen or members of the audit committee and the remuneration committee are available to answer shareholders' questions.

The procedures demanding for a poll and the rights of shareholders to demand for a poll are included in the notice of shareholders' meeting and the accompanying circular. The relevant procedures are explained at the shareholders' meetings.

The external auditor has been appointed as the scrutineer to ensure the votes cast are properly counted and recorded.

The results of the poll have been posted on the website of the GEM on the business day following the meeting.

Furthermore, the Company continues to enhance the ongoing communications amongst the shareholders, investors and analysts, including:

➢ establishing specialized bodies and employing staff to serve investors and analysts and answer their relevant questions;

➢ arranging site visits to the production bases of the Company in order to keep them abreast of the operations and the latest developments of the Company;

➢ collecting and analyzing, in a timely manner, the respective opinions and recommendations on the operations of the Company given by securities analysts and investors and compiling them into reports periodically, and selectively adopting them in the operations of the Company;

➢ providing relevant information, including introduction to the Company, the Board and corporate governance, results of the Company, financial summary, marketing materials of the Company and press releases on the website of the Company; and

➢ taking the initiative to communicate with various parties, particularly following the announcement of interim, annual results and substantial investment decisions, organizing briefings, press conferences and one-on-one interviews with investment institutions. Besides, the Company also regularly communicates with investors on a one-on-one basis.

# Profile of Directors and Senior Management

## Directors

### Executive Directors

Mr. Zhang Hua Wei, aged 43, is the vice chairman and general manager of the Company and vice chairman of Weigao Holding. Mr. Zhang studied politics and economics at the Weihai Campus of Shandong University from 1996 to 1998. Mr. Zhang was the deputy factory director of Weigao Holding from 1988 to 1998, and has been the general manager of Weigao Holding since 1998. Mr. Zhang joined the Company in December 2000.

Mr. Miao Yan Guo, aged 44, is an executive Director and deputy general manager of research and development of the Company. Mr. Miao studied Business Administration at the Weihai Campus of Shandong University from 1999 to 2001. Mr. Miao joined Weigao Holding in 1988 and was sales director from 1988 to 1991, operating manager from 1991 to 1993 and head of the No. 1 branch of Weigao Holding from 1993 to 1998. He was a deputy general manager of Weigao Holding from 1998 to 2000. Mr. Miao joined the Company in December 2000.

Mr. Wang Yi, aged 47, is an executive Director and deputy general manager of general affairs of the Company. Mr. Wang studied Business Administration at the Shandong Cadres Distance Learning University from 1994 to 1997. He joined Weigao Holding in 1988 and was production director from 1988 to 1989, head of the No. 2 branch of Weigao Holding from 1989 to 1992 and manager of the No. 3 branch of Weigao Holding from 1992 to 2004 of sales. Mr. Wang joined the Company in December 2000.

Mr. Wang Zhi Fan, aged 51, is an executive Director and deputy general manager of sales of the Company. He joined Weigao Holding in 1988 and was the production head and the manager of foreign trade of Weigao Holding. Mr. Wang joined the Group in December 2000.

Mr. Wu Chuan Ming, aged 48, is an executive Director and deputy general manager of production of the Company. Mr. Wu joined Weigao Holding in 1988. He has been the manager of the blood transfusion branch from 1996 to 2004. He joined the Group in December 2000.

### Non-executive Directors

Mr. Chen Xue Li, aged 55, is the Chairman of both the Company and Weigao Holding. Mr. Chen founded Weigao Holding in 1988, and was the head of it from 1988 to 1998, Mr. Chen has been elected as the chairman of the Company since December 2000. He received the award of Entrepreneur of Weihai Economy Development in June 2003.

Mrs. Zhou Shu Hua, aged 50, is a non-executive Director of the Company and financial deputy general manager of Weigao Holding. Mrs. Zhou studied Business Administration at the Weihai Campus of Shandong University from 1999 to 2001. Mrs. Zhou joined Weigao Holding in 1989 and held a number of positions such as head of the finance division in the finance department, manager of the finance department and deputy general manager of Weigao Holding.

## Independent non-executive Directors

Mr. Shi Huan, aged 70, is an independent non-executive Director. Mr. Shi is the president of China Pharmaceutical Association of Plant Engineering, a senior engineer and a former deputy head of State Pharmaceutical Administrative Bureau. He was appointed as an independent non-executive Director in September 2002.

Mr. Luan Jian Ping, aged 53, is an independent non-executive Director. Mr. Luan studied philosophy and logic at the People's University of China from 1979 to 1986. He also studied Business Administration at the Aston University in the United Kingdom from 1992 to 1994. He obtained a PRC Lawyer's License issued by the Ministry of Justice of the PRC in October 1996 and is currently a partner of Beijing De Run Law Firm. He was appointed as an independent non-executive Director of the Company in September 2002.

Mr. Lau Wai Kit, aged 43, holds a Bachelor of Law degree and a Postgraduate Certificate in Law from the University of Hong Kong. Mr. Lau is a partner of Gobi Partners, Inc. He was appointed as the financial director and financial controller of two private companies, responsible for the financial management of these companies from 1998 to 2001. Mr. Lau has over sixteen years of experience in practising law, and is a solicitor of the High Court of Hong Kong, an attorney and counselor at law of the Supreme Court of the State of California. Mr. Lau is also the Chairman of Diamondlite Group, a jewelry manufacturer headquartered in Hong Kong. He is also an independent non-executive director of Tianjin Development Holdings Limited and China Insurance International Holdings Company Limited. He sits on the Small Entrepreneur Research Assistance Programme Project Assessment Panel of the Government of the Hong Kong Special Administrative Region. He was appointed as an independent non-executive Director of the Company in November 2004.

Mr. Li Jia Miao, aged 67, is an independent non-executive Director. Mr. Li is a senior economist and obtained a degree in economics and management in Hohai University in 1998. Mr. Li has over 30 years of pharmaceutical related management experiences and has been an assistant general manager and a general manager in Nanjing Pharmaceutical Company since he joined NPC in 1965. Prior to the retirement of Mr. Li in 2005, he was the chairman of Nanjing Pharmaceutical Company Limited since 2000. He was formally appointed as an independent non-executive director of the Company on 28 February 2007.

## Supervisors

The Company has a committee of Supervisors whose primary duty is to supervise the senior management of the Company, including the Board, Directors, managers and other senior officers. The function of the committee of Supervisors is to ensure that the senior management of the Company acts in the interests of the Company, and does not violate the rights of the Company's shareholders and employees. The committee of Supervisors reports to the shareholders in general meetings. The articles of association provides that the committee of Supervisors has the right to investigate the Group's financial affairs; to supervise the directors, general manager and other senior officers of the Company in the event that they contravene any laws, administrative regulations or the articles of association in the performance of their duties; to require the Directors, general manager and other senior management to rectify any activities committed by them that is harmful to the interests of the Company; to examine financial reports, result reports, profit distribution plans and other financial documents prepared by the Board to be submitted to shareholders in general meeting, and in appropriate cases, to appoint certified accountants or certified practicing auditors in the name of the Company to assist in such review; to propose the convening of extraordinary general meetings of shareholders; to represent the Company during negotiations with the Directors or to initiate legal proceedings against the Directors; and other functions and powers given by the shareholders in general meeting. The committee of Supervisors currently comprises the following three members:

Ms. Bi Hong Mei, aged 43, is a supervisor of the Company and the director of the purchase department. Ms. Bi graduated from the Economic Management Department of Shandong Cadres Distance Learning University in 1997. She joined Weigao Holding in December 1988 and has been the head of the finance division and the deputy manager of the infusion sets branch from 2001 to 2004. She joined the Company in December 2000.

Mr. Miao Hai Sheng, aged 34, is a supervisor of the Company and the project manager of auxiliary pre-filled syringe branch. Mr. Miao graduated from the Weihai Campus of Shandong University in 1997, majoring in operation management. He joined Weigao Holding in 1991 and has been the accountant, finance director, the labour and management officer of Weigao Holding. He joined the Company in December 2000.

Ms. Chen Xiao Yun, aged 33, is a supervisor of the Company and the manager of marketing and finance department. Ms. Chen studied financial accounting at the Shandong Broadcast and Television University from 1994 to 1998. She joined Weigao Holding in July 1991 and was the head of the finance division in finance department and the assistant to the manager of infusion sets branch. She joined the Company in December 2000.

## Senior Management

Mr. Jiang Qiang, aged 34, is the deputy general manager of the Company. Mr. Jiang obtained a Master degree in Accounting from Northeast University of Finance and Economics in the PRC in 1998. He is a certified public accountant and has extensive experience in accounting and financial management. Mr. Jiang joined the Company in June 2002.

Mr. Li Yi, aged 42, is the head of production department of the Company and a senior engineer. Mr. Li was graduated from Wuhan Academy of Iron and Steel, major in industrial automation, and has a bachelor degree in engineering. He joined Weigao Holding in 1993 and has been the head of the No.1 Branch Factory of Weigao Holding (from 1993 to 1995), deputy manager, manager of the syringe branch company of Weigao Holding (from 1995 to 2005). Mr. Li joined the Company in December 2000.

Mr. Song Xiushan, aged 43, is the head of sales department of the Company. Mr. Song was graduated from Shandong University, major in corporate administration in 2001, and studied in an advanced business administration program administered by the People University of China from 2002 to 2004. Mr. Song joined Weigao Holding in June 1992, and has been the manager of the Beijing sales branch of Weigao Holding, marketing manager of infusion device branch of Weigao Holding, and has extensive experience in corporate marketing. He joined the Company in December 2000.

Ms. Chan Yuk Ying, Phyllis, aged 46, is the qualified accountant of the Company. Ms. Chan is a chartered accountant with the Institute of Chartered Accountants in Australia and joined the Company in May 2006. Ms. Chan has over 13 years of experience in accounting and corporate finance.

Ms. Wong Miu Ling, Phillis, aged 38, is the company secretary of the Company. Ms. Wong joined the Company in May 2006. She is an associate member of both the Hong Kong Institute of Chartered Secretaries and the Institute of Chartered Secretaries and Administrators. Ms. Wong has over 10 years of experience in corporate finance and management.

The Directors present their annual report and the audited financial statements of the Group for the year ended 31 December 2006.

The Company was established and registered as a joint stock company with limited liability in the PRC under the Company Law of the PRC on 28 December 2000. The shares of the Company were listed on GEM board of the Stock Exchange of Hong Kong Limited on 27 February 2004.

## PRINCIPAL ACTIVITIES

The Company is principally engaged in research, development, production and sale of medical device and has launched over approximately 120 products types with over 2,000 specifications in the market. The principal products types include single use medical consumables, including infusion/transfusion sets, syringes, blood segregator consumable and high valued added products including orthopedic products, blood purification consumables and cardiovascular stent.

## RESULTS AND DIVIDENDS

The results of the Group for the year ended 31 December 2006 are set out in the consolidated income statement on page 46 of this annual report.

An interim dividend of RMB 2 cents per share amounting to approximately RMB19,311,000 was paid during the year. The Directors now recommend the payment of a final dividend of RMB 3.3 cents per shares to the shareholders on the register of members on 9 May 2007 amounting to approximately RMB 31,863,000 and the retention of the remaining profit for the year of approximately RMB 76,424,000.

## PROPERTY, PLANT AND EQUIPMENT

The Group acquired property, plant and equipment during the year of 2006 at an aggregate cost of approximately RMB 162,856,000 (including RMB45,000,000 being the deposit for acquisition of property) in order to enhance its production capacity. Details of movements in the property, plant and equipment of the Group are set out in note 13 to the financial statements.

## SHARE CAPITAL

There were no movements in either the Company's authorised or issued share capital during the year.

## DISTRIBUTABLE RESERVES OF THE COMPANY

As at 31 December 2006, an amount of approximately RMB108,287,000 (2005: RMB 101,201,000) standing to the credit of the Company's reserve account, which is computed based on the lower of , (i) in accordance with the PRC accounting standards and regulation, the aggregate amount of profit after taxation for the year and (ii) in accordance with Hong Kong accounting standards and regulation, the retained profit brought forward after deduction of the current year's appropriation to the statutory surplus reserve and statutory public welfare fund.

## DIRECTORS AND DIRECTORS' SERVICE CONTRACTS

The directors of the Company during the year were:

### EXECUTIVE DIRECTORS:

Mr. Zhang Hua Wei
Mr. Miao Yan Guo
Mr. Wang Yi
Mr. Wang Zhi Fan
Mr. Wu Chuan Ming

### NON-EXECUTIVE DIRECTORS

Mr. Chen Xue Li
Mrs. Zhou Shu Hua

### INDEPENDENT NON-EXECUTIVE DIRECTORS

Mr. Lau Wai Kit
Mr. Luan Jian Ping
Mr. Shi Huan
Mr. Li Jia Miao (appointed on 28 February 2007)

Each of the executive and non-executive directors (except for Mr. Luan Jian Ping and Mr. Shi Huan, the two independent non-executive directors who entered into service agreements with the Company on 1 September 2002 and Mr. Lau Wai Kit, an independent non-executive director who entered into a service agreement with the Company on 1 September 2004) entered into a service agreement with the Company on 11 February 2004, commencing on 27 February 2004 for an initial term of three years, unless and until terminated by either party by giving notice to the other party not less than three months' time in writing. In accordance with the Company's articles of association, the service agreements of all directors are renewable for successive three-year terms.

The service agreements for executive and non-executive directors do not stipulate for any amount of remuneration or bonus payment to be paid for services provided. The executive and non-executive directors are paid with a fixed sum of annual salaries for holding positions in the Company. All executive and non-executive directors shall be entitled to welfare benefits (including retirement benefits and medical insurance) in accordance with the relevant laws and regulations in the PRC. According to the service agreement entered into between the Company and each of the three independent non-executive directors, Mr. Luan Jian Ping and Mr. Shi Huan shall received nominal fee of RMB30,000 Mr. Lau Wai Kit, another independent non-executive director, is also a partner of Gobi Partners, Inc. ("Gobi"), a China-based venture capital firm. He waived his director's remuneration of RMB 48,000 for the year ended 31 December 2006 and instead took a nominal annual fee of RMB1.00 to comply with Gobi's internal compliance requirements.

Apart from the foregoing, no directors have 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' INTERESTS IN CONTRACTS

No director, either directly or indirectly, in any contract of significance to the business of the Group to which the Company, its holding company, or any of its subsidiaries or fellow subsidiaries was a party during the year.

## INDEPENDENCE OF INDEPENDENT NON-EXECUTIVE DIRECTORS

The Company has received, from each of the independent non-executive directors, an annual confirmation of his independence pursuant to Rule 5.09 of the GEM Listing Rules. The Company considers all of the independent non-executive directors are independent.

## DIRECTORS' INTERESTS AND LONG POSITIONS IN SHARES

As at 31 December 2006, the interests of the directors in the share capital of the Company and their associated corporations (within the meaning of Part XV of the Securities and Futures Ordinance (the "SFO")), as recorded in the registered required to be kept by the Company pursuant to Section 352 of the SFO, or as otherwise notified to the Company and the Stock Exchange pursuant to the Model Code for Securities Transactions by Directors of Listed Companies of Rule 5.46 of the GEM Listing Rules, were as follows:

(i) Long positions of domestic shares of RMB0.10 each of the Company

| Name of director | Capacity | Number of domestic shares | Approximate percentage of the Company's issued share capital |
|---|---|---|---|
| Mr. Zhang Hua Wei | Beneficial owner | 10,800,000 | 1.12% |
| Mr. Miao Yan Guo | Beneficial owner | 7,800,000 | 0.81% |
| Mr. Wang Yi | Beneficial owner | 7,800,000 | 0.81% |
| Mrs. Zhou Shu Hua | Beneficial owner | 5,100,000 | 0.53% |
| Mr. Wang Zhi Fan | Beneficial owner | 2,700,000 | 0.28% |
| Mr. Wu Chuan Ming | Beneficial owner | 2,400,000 | 0.25% |

(ii) Long positions in the registered capital of the ultimate holding company, Weigao Holding, an associated corporation of the Company

| Name of director | Capacity | Amount of registered capital | Approximate percentage of the registered capital of Weigao Holding |
|---|---|---|---|
| Mr. Chen Xue Li | Beneficial owner | 36,600,000 | 30.00% |
| Mr. Zhang Hua Wei | Beneficial owner | 29,280,000 | 24.00% |
| Mrs. Zhou Shu Hua | Beneficial owner | 14,579,000 | 11.95% |
| Mr. Miao Yan Guo | Beneficial owner | 7,320,000 | 6.00% |
| Mr. Wang Yi | Beneficial owner | 7,320,000 | 6.00% |
| Mr. Wang Zhi Fan | Beneficial owner | 2,610,800 | 2.14% |
| Mr. Wu Chuan Ming | Beneficial owner | 2,257,000 | 1.85% |

Other than as disclosed above, none of the Directors nor their associates had any interests or short positions in any shares of the Company or any of its associated corporations as at the date of this report.

## PURCHASE, SALE OR REDEMPTION OF SECURITIES

At no time during the year were rights to acquire benefits by means of the acquisition of shares in or debenture of the Company granted to any directors or their respective associates or were any such rights exercised by them; or was the Company, its ultimate holding company or any subsidiaries of its ultimate holding company or fellow subsidiaries a party to any arrangement to enable the directors of the Company to acquire such rights in the Company or any other body corporate.

## SUBSTANTIAL SHAREHOLDERS

As at 31 December 2006, the register of substantial shareholders maintained by the Company pursuant to Section 336 of the SFO recorded that other than the interests disclosed above in respect of certain Directors, the following shareholder had notified the Company of relevant interest in the issued share capital of the Company.

| Name of shareholder | Capacity | Number of domestic shares | Approximate percentage of the Company's issued share capital |
|---|---|---|---|
| Weigao Holding | Beneficial owner | 578,160,000 | 59.88% |

Save as disclosed above, the Company has not been notified of any other relevant interests or short positions in the issued share capital of the Company as at 31 December 2006.

## MAJOR CUSTOMERS AND SUPPLIERS

In the year under review, sales to the Group's five largest customers accounted for 4.08% of the total sales for the year and sales to the largest customer included therein accounted for 0.93% of the total sales of the year. Purchases from the Group's five largest suppliers accounted for 23.16% of the total purchases for the year and purchases to the largest supplier included therein accounted for 6.74% of the total sales of the year. During the year, none of the directors of the Company or any of their associates or any shareholders (which to the knowledge of the directors, own more than 5% of the Company's issued share capital) had any beneficial interest in the top five customers and suppliers of the Group.

## PRE-EMPTIVE RIGHTS

There are no provisions for pre-emptive right under the Company's articles of association, or the laws in the PRC, which would oblige the Company to offer new shares on a pro-rata basis to existing shareholders.

## COMPETITION AND CONFLICT OF INTERESTS

None of the Directors or the management shareholders as defined under the "GEM Listing Rules" of the Company or their respective associates has any interest in a business which competes or may compete with the business of the Group or has any other conflict of interests with the Group.

## COMPLIANCE ADVISER'S INTERESTS

Goldbond Capital (Asia) Limited ("Goldbond") has been appointed as the compliance adviser of the Company from 24 July 2004 to 31 December 2006 and the term of engagement has been extended to the date of release of financial results of 2006 pursuant to a letter dated 19 January 2007.

Neither Goldbond, nor its Directors or employees or associates (as referred to in note 3 to Rule 6.35 of the GEM Listing Rules) had any interest in the share capital of the Company or any other companies in the Group as at 31 December 2006.

## CONNECTED TRANSACTIONS

The connected transactions between the Company, Weigao Holding and its subsidiary during the year under review are as follows:

## NON-EXEMPT CONNECTED TRANSACTIONS

A. The Company and its fellow subsidiary, Weigao Medical Material Co., Ltd ("Weigao Medical") entered into a sub manufacturing contract on 27 January 2004. Under the sub-manufacturing contract, Weigao Medical is responsible for procuring the raw materials and the manufacturing of certain products and spare parts in compliance with national quality and hygiene standards of the Company.

   For the year ended 31 December 2006, the Company sub-contracted the processing of various spare parts and the products to Weigao Medical at the price as agreed in the contract. The total processing cost amounted to approximately RMB198,000.

B. On 12 August 2005, the Company entered into a property rental agreement with Shandong Weigao Biosensors Medical Products Company Limited ("Weigao Biosensors"), 50% owned by Weigao Holding, for an annual rental of approximately RMB1,496,000 for a term of three years commencing 12 August 2005.

   For the year under review, the Company received an annual rental of approximately RMB1,496,000 from Weigao Biosensors at the agreed rent as set out in the lease agreement.

C. On 21 December 2004, Weihai Jierui Medical Products Company Limited ("Jierui Subsidiary"), a 96%- owned subsidiary of the Company entered into the packaging material agreement (the "Agreement") with Shandong Weigao Pharmaceutical Company Limited ("Weigao Pharmaceutical") 48.6% owned by Weigao Holding, for the sales of mainly packaging materials from Jierui Subsidiary to Weigao Pharmaceutical for an annual transaction amount of not more than RMB 1,000,000 for the contract period from 1 January 2005 to 31 December 2006. On 18 April 2006, Jierui Subsidiary entered into the Supplemental Agreement with Weigao Pharmaceutical pursuant to which the maximum annual transaction amount was increased to more than RMB 9,000,000, the unit selling prices of the various items listed in the Agreement were adjusted with reference to the latest market unit prices, the number of items listed under the Agreement was increased and the contract period of the Agreement was extended to 31 December 2008.

   For the year under review, the Company received an amount of approximately RMB3,034,000 from Jierui Subsidiary with respect to the Agreement.

D. On 1 November 2006, a legally binding letter of intent ("LOI") was entered into among the Company, Weigao Holding, JW Medical, Biosensors, BSI, BVI Co and Weigao Biosensors regarding equity investment in, licensing of technologies to and option to acquire interests in JW Medical by Biosensors and sale and purchase of equity interests in Weigao Biosensors.

Pursuant to the option agreement dated 4 February 2004 between Weigao Holding and the Company, Weigao Holding granted an option to the Company at the Company's discretion to acquire Weigao Holding's entire interests of 50% in Weigao Biosensors. The exercise price would have been the appraised value of 50% interests as determined by a firm of independent professional valuers with international reputation appointed by the Company. Pursuant to the LOI, the non-exercise of the Weigao Biosensors Option by the Company to acquire 50% equity interests in Weigao Biosensors is construed as a connected transaction for the Company under Rule 20.70(3) of the GEM Listing Rules.

E. On 1 February 2007, 威海威高富森醫用材料有限公司 (Weihai Weigao Fusen Medical Materials Company Limited) ("Weihai Weigao Fusen"), a 70% owned subsidiary of Weigao Holding entered into the agreement with the Company for the sale of surgical suture, medical dressing and surgical tape for an annual transaction amount of not more than RMB 2.0 million for the contract period from 1 February 2007 to 31 January 2008. The annual transaction amount under the agreement will be not more than RMB 2.0 million.

Save as disclosed therein, there were no other material transactions to be disclosed as connected and related party transactions in accordance with the requirements of the GEM Listing Rules and accounting principles generally accepted in Hong Kong.

The directors, including the independent non-executive directors have reviewed the connected transactions above and in their opinion, these transactions entered into by the Group are in the ordinary and usual course of business of the Group, on normal commercial terms and such terms are fair and reasonable so far as the Company and the shareholders of the Company as a whole are concerned and the agreements are in the interest of the Company and the Shareholders of the Company as a whole.

Save as disclosed above, there has been no contract of significance between the Company or its subsidiary and Weigao Holding or any of its subsidiary.

## AUDIT COMMITTEE

The Company set up an audit committee on 1 September 2002 with terms of reference in compliance with Rules 5.28 to 5.33 of the GEM Listing Rules. The primary duties of the audit committee are to review and supervise the financial reporting process and internal control system of the Group. The audit committee has five members comprising Mr. Shi Huan, Mr Luan Jian Ping and Mr. Lau Wai Kit, being independent non-executive directors and Mrs. Zhou Shu Hua, a non-executive director. Mr Li Jia Miao, an independent non-executive directors being appointed as a member of the audit committee on 14 March 2007.

During the year, the audit committee held four meetings and the committee had reviewed and approved the annual report for the year ended 31 December 2005 and the first three quarterly reports of the year 2006. On 13 March 2007, the audit committee had reviewed and approved the financial statements for the year ended 31 December 2006.

The unaudited quarterly and interim results and annual results during the year ended 31 December 2006 have been reviewed by the audit committee, which was of the opinion that the preparation of such results complied with the applicable accounting standards and requirements and that adequate disclosure have been made.

## POST BALANCE SHEET EVENTS

Subsequent to the balance sheet date, the Group has entered into the following significant transactions:

(1) On 2 March 2007, the Company entered into an eight-year long-term loan agreement for US$20 million with the International Finance Corporation, a member of the World Bank Group.

(2) On 11 March 2007, the Company, Weigao Holding and Medtronic have entered into a non binding letter of intent in relation to the proposed investment in the Company by Medtronic of up to 15% of the enlarged issued share capital of the Company in form of a combination of existing domestic shares and to be issued new H shares.

## AUDITORS

A resolution will be proposed at the forthcoming annual general meeting to re-appoint Deloitte Touche Tohmatsu as auditors of the Company.

On behalf of the Board

**Chen Xue Li**
*Chairman*

Weihai, Shandong, the PRC
14 March 2007

Deloitte.
德勤

TO THE MEMBERS OF SHANDONG WEIGAO GROUP MEDICAL POLYMER COMPANY LIMITED
山東威高集團醫用高份子制品股份有限公司
*(A joint stock limited company established in the People's Republic of China)*

We have audited the consolidated financial statements of Shandong Weigao Group Medical Polymer Company Limited (the "Company") and its subsidiaries (collectively referred to as the "Group") set out on pages 47 to 79, which comprise the consolidated balance sheet as at 31st December, 2006, and the consolidated income statement, the consolidated statement of changes in equity and the consolidated cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes.

## Directors' responsibility for the consolidated financial statements

The directors of the Company are responsible for the preparation and the true and fair presentation of these consolidated financial statements in accordance with Hong Kong Financial Reporting Standards issued by the Hong Kong Institute of Certified Public Accountants and the disclosure requirements of the Hong Kong Companies Ordinance. This responsibility includes designing, implementing and maintaining internal control relevant to the preparation and the true and fair presentation of the consolidated financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

## Auditor's responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit 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. We conducted our audit in accordance with Hong Kong Standards on Auditing issued by the Hong Kong Institute of Certified Public Accountants. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance as to whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and true and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the directors, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

## Opinion

In our opinion, the consolidated financial statements give a true and fair view of the state of affairs of the Group as at 31st December, 2006 and of the Group's profit and cash flows for the year then ended in accordance with Hong Kong Financial Reporting Standards and have been properly prepared in accordance with the disclosure requirements of the Hong Kong Companies Ordinance.

**Deloitte Touche Tohmatsu**
*Certified Public Accountants*

Hong Kong
14 March 2007

# Consolidated Income Statement

For the year ended 31st December, 2006

| | NOTES | 2006<br>*RMB'000* | 2005<br>*RMB'000* |
|---|---|---|---|
| Revenue | 5 | **786,926** | 569,987 |
| Cost of sales | | **(451,585)** | (335,727) |
| Gross profit | | **335,341** | 234,260 |
| Other income | | **18,191** | 14,830 |
| Distribution costs | | **(115,368)** | (87,385) |
| Administrative expenses | | **(59,759)** | (40,107) |
| Finance costs | 7 | **(21,519)** | (17,038) |
| Share of profit (loss) of a jointly controlled entity | | **32,462** | (1,457) |
| Share of loss of an associate | | **—** | (523) |
| Profit before taxation | 8 | **189,348** | 102,580 |
| Taxation | 9 | **(6,745)** | (2) |
| Profit for the year | | **182,603** | 102,578 |
| Attributable to: | | | |
| Equity holders of the Company | | **170,921** | 101,200 |
| Minority interests | | **11,682** | 1,378 |
| | | **182,603** | 102,578 |
| Dividends | 11 | | |
| Dividends paid | | **38,622** | 20,366 |
| Dividends proposed | | **31,863** | 19,311 |
| Earnings per share - basic | 12 | **RMB0.18** | RMB0.11 |

# Consolidated Balance Sheet

As 31st December, 2006

| | NOTES | 2006 RMB'000 | 2005 RMB'000 |
|---|---|---|---|
| Non-current assets | | | |
| Property, plant and equipment | 13 | **591,913** | 518,248 |
| Prepaid lease payments | 14 | **53,922** | 55,299 |
| Deposits for property, plant and equipment | | **45,000** | — |
| Interest in a jointly controlled entity | 15 | **43,805** | 11,343 |
| | | **734,640** | 584,890 |
| Current assets | | | |
| Inventories | 16 | **166,185** | 119,369 |
| Trade and other receivables | 17 | **355,835** | 250,329 |
| Pledged bank deposits | 18 | **22,328** | 22,657 |
| Bank balances and cash | 19 | **115,131** | 154,985 |
| | | **659,479** | 547,340 |
| Current liabilities | | | |
| Trade and other payables | 20 | **253,801** | 147,009 |
| Borrowings – repayable within one year | 21 | **105,043** | 177,200 |
| Tax payable | | **6,429** | — |
| | | **365,273** | 324,209 |
| Net current assets | | **294,206** | 223,131 |
| Total assets less current liabilities | | **1,028,846** | 808,021 |
| Capital and reserves | | | |
| Share capital | 22 | **96,556** | 96,556 |
| Reserves | | **602,184** | 469,885 |
| Equity attributable to equity holders of the Company | | **698,740** | 566,441 |
| Minority interests | | **49,106** | 31,580 |
| Total equity | | **747,846** | 598,021 |
| Non-current liability | | | |
| Borrowings – repayable after one year | 21 | **281,000** | 210,000 |
| | | **1,028,846** | 808,021 |

The consolidated financial statements on pages 47 to 79 were approved by the Board of Directors on 14 March 2007 and are signed on its behalf by:

| **Chen Xue Li** | **Zhang Hua Wei** |
|---|---|
| DIRECTOR | DIRECTOR |

# Consolidated Statement of Changes in Equity

For the year ended 31st December, 2006

| | Attributable to equity holders of the Company | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | Share capital RMB'000 | Share premium reserve RMB'000 | Statutory surplus reserve RMB'000 (Note a) | Statutory public welfare fund RMB'000 (Note b) | Retained earnings RMB'000 | Total RMB'000 | Minority interests RMB'000 | Total RMB'000 |
| At 1st January 2005 | 86,450 | 126,848 | 19,560 | 9,780 | 125,959 | 368,597 | 8,920 | 377,517 |
| Issue of domestic shares | 4,816 | 42,184 | — | — | — | 47,000 | — | 47,000 |
| Issue of H shares | 5,290 | 69,053 | — | — | — | 74,343 | — | 74,343 |
| Share issue expenses | — | (4,333) | — | — | — | (4,333) | — | (4,333) |
| Profit for the year and total recognised income | — | — | — | — | 101,200 | 101,200 | 1,378 | 102,578 |
| Dividend paid | — | — | — | — | (20,366) | (20,366) | — | (20,366) |
| Appropriation | — | — | 14,733 | 7,367 | (22,100) | — | — | — |
| Acquisition of subsidiaries | — | — | — | — | — | — | 15,974 | 15,974 |
| Capital contribution from minority interests | — | — | — | — | — | — | 5,308 | 5,308 |
| At 31st December 2005 | 96,556 | 233,752 | 34,293 | 17,147 | 184,693 | 566,441 | 31,580 | 598,021 |
| Profit for the year and total recognised income | — | — | — | — | 170,921 | 170,921 | 11,682 | 182,603 |
| Dividend paid | — | — | — | — | (38,622) | (38,622) | — | (38,622) |
| Appropriation | — | — | 36,033 | (17,147) | (18,886) | — | — | — |
| Acquisition of additional interests in subsidiaries | — | — | — | — | — | — | (3,713) | (3,713) |
| Capital contribution from minority interests | — | — | — | — | — | — | 9,557 | 9,557 |
| At 31st December 2006 | 96,556 | 233,752 | 70,326 | — | 298,106 | 698,740 | 49,106 | 747,846 |

*Notes:*

(a) The Articles of Association of the companies comprising the Group except Weigao International Medical Co. Limited ("Weigao International") require the appropriation of 10% of profit after taxation (prepared under the generally accepted accounting principles in the PRC) each year to the statutory surplus reserve until the balance reaches 50% of the registered share capital. According to the provisions of the Articles of Association of the companies comprising the Group, in normal circumstances, the statutory surplus reserve shall only be used for making up losses, capitalisation into share capital and expansion of its production and operation. For the capitalisation of statutory surplus reserve into share capital, the remaining amount of such reserve shall not be less than 25% of the registered share capital.

(b) Pursuant to the PRC Company Law, the companies comprising the Group except Weigao International shall make allocation from profit after taxation (prepared under the generally accepted accounting principles in the PRC) at the rate of 5% to 10% to the statutory public welfare fund (see below). The statutory public welfare fund can only be used on the capital items for employees collective welfare. Individual employees only have the right to use these facilities and the titles on which will remain with the Group. The statutory public welfare fund is non-distributable other than in liquidation.

From 1st January 2006, according to the revised PRC Company Law, the companies comprising the Group except Weigao International are not required to make such transfers. The directors of the Company resolved to transfer the statutory public welfare fund of RMB17,147,000 as at 1st January 2006 to statutory surplus reserve which is in compliance with the PRC Company Law.

# Consolidated Cash Flow Statement

For the year ended 31st December, 2006

| | NOTE | 2006 RMB'000 | 2005 RMB'000 |
|---|---|---|---|
| OPERATING ACTIVITIES | | | |
| Profit before taxation | | **189,348** | 102,580 |
| Adjustments for: | | | |
| Interest income | | **(751)** | (589) |
| Interest expense | | **21,519** | 17,038 |
| Depreciation | | **43,308** | 23,863 |
| Prepaid lease payments charged to income | | **1,377** | 1,305 |
| Allowances for bad and doubtful debts | | **5,747** | 3,862 |
| Share of (profit) loss of a jointly controlled entity | | **(32,462)** | 1,457 |
| Share of loss of an associate | | **—** | 523 |
| Loss on disposals of property, plant and equipment | | **54** | 378 |
| Operating profit before working capital changes | | **228,140** | 150,417 |
| Increase in inventories | | **(46,816)** | (35,759) |
| Increase in trade and other receivables | | **(111,253)** | (74,114) |
| Increase in trade and other payables | | **106,792** | 30,126 |
| Net cash generated from operations | | **176,863** | 70,670 |
| PRC income tax paid | | **(316)** | (1,938) |
| NET CASH GENERATED FROM OPERATING ACTIVITIES | | **176,547** | 68,732 |
| INVESTING ACTIVITIES | | | |
| Purchase of property, plant and equipment | | **(110,356)** | (165,156) |
| Prepaid lease payments | | **—** | (4,560) |
| Deposit for property, plant and equipment | | **(45,000)** | — |
| Acquisition of subsidiaries | 23 | **—** | 9,889 |
| Acquisition of additional interests in subsidiaries | | **(3,713)** | — |
| Acquisition of investment in an associate | | **—** | (8,000) |
| Proceeds from disposal of property, plant and equipment | | **829** | 5,517 |
| Interest received | | **751** | 589 |
| Decrease (increase) in pledged bank deposits | | **329** | (13,657) |
| NET CASH USED IN INVESTING ACTIVITIES | | **(157,160)** | (175,378) |

# Consolidated Cash Flow Statement

For the year ended 31st December, 2006

| | **2006** | 2005 |
|---|---|---|
| | ***RMB'000*** | *RMB'000* |
| FINANCING ACTIVITIES | | |
| New borrowings raised | **432,043** | 441,886 |
| Issue of shares | **—** | 74,343 |
| Share issue expenses | **—** | (4,333) |
| Repayments of borrowings | **(433,200)** | (329,850) |
| Capital contributions from minority interests | **2,057** | 5,308 |
| Interest paid | **(21,519)** | (17,038) |
| Dividend paid | **(38,622)** | (20,366) |
| NET CASH (USED IN) GENERATED FROM FINANCING ACTIVITIES | **(59,241)** | 149,950 |
| NET (DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS | **(39,854)** | 43,304 |
| CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR | **154,985** | 111,681 |
| CASH AND CASH EQUIVALENTS AT END OF YEAR, representing bank balances and cash | **115,131** | 154,985 |

## 1. GENERAL

The Company was established and registered as a joint stock company with limited liability in the People's Republic of China (the "PRC") under the Company Law of the PRC on 28th December 2000. Its ultimate holding company is Weigao Holding Company Limited (formally known as Shandong Weigao Group Company Limited) ("Weigao Holding"), a company registered in the PRC with limited liability. The address of the registered office and principal place of business of the Company is at 312 Shi Chang Road, Weihai, Shandong Province, PRC.

The Company's shares have been listed on the Growth Enterprise Market ("GEM") of The Stock Exchange of Hong Kong Limited (the "Stock Exchange") since 27th February 2004.

The Company and its subsidiaries (hereinafter collectively referred to as the "Group") are principally engaged in the research and development, production and sale of single-use medical devices.

The consolidated financial statements are presented in Renminbi ("RMB"), which is the functional currency of the Company.

## 2. APPLICATION OF NEW AND REVISED HONG KONG FINANCIAL REPORTING STANDARDS ("HKFRSs")

In the current year, the Group has applied, for the first time, a number of new standards, amendments and interpretations ("new HKFRSs") issued by the Hong Kong Institute of Certified Public Accountants ("HKICPA"), which are either effective for accounting periods beginning on or after 1st December 2005 or 1st January 2006. The adoption of the new HKFRSs had no material effect on how the results and financial position for the current or prior accounting periods have been prepared and presented. Accordingly, no prior period adjustment has been required.

The Group has not early applied the following new standard, amendment or interpretations that have been issued but are not yet effective. The directors of the Company anticipate that the application of these new standard, amendment or interpretations will have no material impact on the results and financial position of the Group.

| | |
|---|---|
| HKAS 1 (Amendment) | Capital disclosures [1] |
| HKFRS 7 | Financial instruments: Disclosures [1] |
| HK(IFRIC) - INT 7 | Applying the restatement approach under HKAS 29 Financial Reporting in Hyperinflationary Economies [2] |
| HK(IFRIC) - INT 8 | Scope of HKFRS 2 [3] |
| HK(IFRIC) - INT 9 | Reassessment of embedded derivatives [4] |
| HK(IFRIC) - INT 10 | Interim financial reporting and impairment [5] |
| HK(IFRIC) - INT 11 | HKFRS 2 - Group and treasury share transactions [6] |

[1] Effective for annual periods beginning on or after 1st January 2007.
[2] Effective for annual periods beginning on or after 1st March 2006.
[3] Effective for annual periods beginning on or after 1st May 2006.
[4] Effective for annual periods beginning on or after 1st June 2006.
[5] Effective for annual periods beginning on or after 1st November 2006.
[6] Effective for annual periods beginning on or after 1st March 2007.

## 3. SIGNIFICANT ACCOUNTING POLICIES

The consolidated financial statements have been prepared on the historical cost basis.

The consolidated financial statements have been prepared in accordance with HKFRSs issued by the HKICPA. In addition, the consolidated financial statements include applicable disclosures required by the Rules Governing the Listing of Securities on the GEM of the Stock Exchange and by the Hong Kong Companies Ordinance.

### BASIS OF CONSOLIDATION

The consolidated financial statements incorporate the financial statements of the Company and entities (including special purpose entities) controlled by the Company (its subsidiaries). Control is achieved where the Company has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities.

The results of subsidiaries acquired or disposed of during the year are included in the consolidated income statement from the effective date of acquisition or up to the effective date of disposal, as appropriate.

Where necessary, adjustments are made to the financial statements of subsidiaries to bring their accounting policies into line with those used by other members of the Group.

All intra-group transactions, balances, income and expenses are eliminated on consolidation.

Minority interests in the net assets of consolidated subsidiaries are presented separately from the Group's equity therein. Minority interests in the net assets consist of the amount of those interests at the date of the original business combination and the minority's share of changes in equity since the date of the combination. Losses applicable to the minority in excess of the minority's interest in the subsidiary's equity are allocated against the interests of the Group except to the extent that the minority has a binding obligation and is able to make an additional investment to cover the losses.

Acquisition of additional interests in subsidiaries are recorded at historical cost and the excess of the cost of acquisition over the carrying amounts of net assets acquired is recognised as goodwill. Such goodwill is carried at cost less any accumulated impairment losses.

### BUSINESS COMBINATIONS

The acquisition of subsidiaries is accounted for using the purchase method. The cost of the acquisition is measured at the aggregate of the fair values, at the date of exchange, of assets given, liabilities incurred or assumed, and equity instruments issued by the Group in exchange for control of the acquiree, plus any costs directly attributable to the business combination. The acquiree's identifiable assets, liabilities and contingent liabilities are recognised at their fair values at the acquisition date.

The interest of minority shareholders in the acquiree is initially measured at the minority's proportion of the net fair value of the assets, liabilities and contingent liabilities recognised.

## 3. SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

### REVENUE RECOGNITION

Revenue is measured at fair value of the consideration received or receivable and represents amounts receivable for goods provided in the normal course of business, net of discounts and sales related taxes.

Revenue from sales of medical products are recognised when the medical products are delivered and title has passed.

Interest income from a financial asset is accrued on a time basis, by reference to the principal outstanding and at the effective interest rate applicable, which is the rate that exactly discounts the estimated future cash receipts through the expected life of the financial asset to that asset's net carrying amount.

Rebate of value added tax is recognised when it is entitled to receive.

### RESEARCH AND DEVELOPMENT EXPENDITURE

Expenditure on research activities is recognised as an expense in the year in which it is incurred.

An internally-generated intangible asset arising from development expenditure is recognised only if it is anticipated that the development costs incurred on a clearly-defined project will be recovered through future commercial activity. The resultant asset is amortised on a straight-line basis over its useful life, and carried at cost less subsequent accumulated amortisation and any accumulated impairment loss.

Where no internally-generated intangible asset can be recognised, development expenditure is charged to profit or loss in the period in which it is incurred.

### RETIREMENT BENEFIT COSTS

Payments to Mandatory Provident Fund Scheme and state-managed retirement benefits schemes are charged as expenses as they fall due.

## 3. SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

### TAXATION

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 profit as reported in the consolidated 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 or deductible. The Group's liability for current tax is calculated using tax rates that have been enacted or satisfactorily enacted by the balance sheet date.

Deferred tax is recognised on differences between the carrying amounts of assets and liabilities in the consolidated 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 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 year when the liability is settled or the asset realised. Deferred tax is charged or credited to profit or loss, except when it relates to items charged or credited directly to equity, in which case the deferred tax is also dealt with in equity.

### PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment, other than construction in progress, are stated at cost less accumulated depreciation and accumulated impairment loss.

Depreciation is provided to write off the cost of items of property, plant and equipment, other than construction in progress, over their estimated useful lives and after taking into account their estimated residual value, using the straight-line method.

Construction in progress is stated at cost which includes all development expenditure and other direct costs attributable to such projects. Costs on completed construction work are transferred to the appropriate category of property, plant and equipment. No depreciation is provided on construction in progress until the construction is completed and the relevant assets are available for use.

An item of property, plant and equipment is derecognised upon disposal or when no future economic benefits are expected to arise from the continued use of the asset. Any gain or loss arising on derecognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the item) is included in the consolidated income statement in the year in which the item is derecognised.

## 3. SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

### INTEREST IN A JOINTLY CONTROLLED ENTITY

Joint venture arrangements that involve the establishment of a separate entity in which venturers have joint control over the economic activity of the entity are referred to as jointly controlled entities.

The results and assets and liabilities of jointly controlled entities are incorporated in the consolidated financial statements using the equity method of accounting. Under the equity method, investments in jointly controlled entities are carried in the consolidated balance sheet at cost as adjusted for post-acquisition changes in the Group's share of the profit or loss and of changes in equity of the jointly controlled entities, less any identified impairment loss. When the Group's share of losses of a jointly controlled entity equals or exceeds its interest in that jointly controlled entity (which includes any long-term interests that, in substance, form part of the Group's net investment in the jointly controlled entity), the Group discontinues recognising its share of further losses. An additional share of losses is provided for and a liability is recognised only to the extent that the Group has incurred legal or constructive obligations or made payments on behalf of that jointly controlled entity.

When a group entity transacts with a jointly controlled entity of the Group, unrealised profits or losses are eliminated to the extent of the Group's interest in the jointly controlled entity, except to the extent that unrealised losses provide evidence of an impairment of the asset transferred, in which case, the full amount of losses is recognised.

### INVENTORIES

Inventories are stated at the lower of cost and net realisable value. Cost is calculated using the weighted average cost method. Net realisable value represents the estimated selling price less all estimated costs of completion and costs to be incurred in marketing, selling and distribution.

### IMPAIRMENT

At each balance sheet date, the Group reviews the carrying amounts of its tangible assets to determine whether there is any indication that those assets have suffered an impairment loss. If the recoverable amount of an asset is estimated to be less than its carrying amount, the carrying amount of the asset is reduced to its recoverable amount. An impairment loss is recognised as an expense immediately.

Where an impairment loss subsequently reverses, the carrying amount of the asset is increased to the revised estimate of its recoverable amount, such that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset in prior years. A reversal of an impairment loss is recognised as income immediately.

## 3. SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

### LEASING

Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating leases.

*The Group as lessor*

Rental income from operating leases is recognised in the consolidated income statement on a straight-line basis over the term of the relevant lease. Initial direct costs incurred in negotiating and arranging an operating lease are added to the carrying amount of the leased asset and recognised as an expense on a straight-line basis over the lease term.

*The Group as lessee*

Rentals payable under operating leases are charged to profit or loss on a straight-line basis over the term of the relevant lease. Benefits received and receivable as an incentive to enter into an operating lease are recognised as a reduction of rental expense over the lease term on a straight-line basis.

### BORROWING COST

All borrowing costs are recognised as and included in finance costs in the consolidated income statement in the period in which they are incurred.

### FOREIGN CURRENCIES

In preparing the financial statements of each individual group entity, transactions in currencies other than the functional currency of that entity (foreign currencies) are recorded in the respective functional currency (i.e. the currency of the primary economic environment in which the entity operates) at the rates of exchanges prevailing on the dates of the transactions. At each balance sheet date, monetary items denominated in foreign currencies are retranslated at the rates prevailing on the balance sheet date. Non-monetary items that are measured in terms of historical cost in a foreign currency are not retranslated.

Exchange differences arising on the settlement of monetary items, and on the translation of monetary items, are recognised in profit or loss in the period in which they arise.

## 3. SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

### FINANCIAL INSTRUMENTS

Financial assets and financial liabilities are recognised on the balance sheet when a group entity becomes a party to the contractual provisions of the instrument and are initially measured at fair value.

Transaction costs that are directly attributable to the acquisition or issue of financial assets and financial liabilities are added to or deducted from the fair value of the financial assets or financial liabilities, as appropriate, on initial recognition.

*Trade and other receivables, bank balances and pledged bank deposits*

Trade and other receivables, bank balances and pledged bank deposits are subsequently measured at amortised cost using the effective interest method. Appropriate allowances for estimated irrecoverable amounts are recognised in profit or loss when there is objective evidence that the asset is impaired. The allowance recognised is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the original effective interest rate.

*Financial liabilities and equity instruments*

Financial liabilities and equity instruments issued by the Group are classified according to the substance of the contractual arrangements entered into and the definitions of a financial liability and an equity instrument. An equity instrument is any contract that evidences a residual interest in the assets of the Group after deducting all of its liabilities. The accounting policies adopted for specific financial liabilities and equity instruments are set out below.

*Borrowings*

Interest-bearing loans are subsequently measured at amortised cost, using the effective interest method.

*Trade and other payables*

Trade and other payables are subsequently measured at amortised cost, using the effective interest method.

*Equity instruments*

Equity instruments issued by the Company are recorded at the proceeds received, net of direct issue costs.

### DERECOGNITION

Financial assets are derecognised when the rights to receive cash flows from the assets expire or, the financial assets are transferred and the Group has transferred substantially all the risks and rewards of ownership of the financial assets. On derecognition of a financial asset, the difference between the asset's carrying amount and the sum of the consideration received and receivable and the cumulative gain or loss that had been recognised directly in equity is recognised in profit or loss.

Financial liabilities are derecognised when the obligation specified in the relevant contract is discharged, cancelled or expires. The difference between the carrying amount of the financial liability derecognised and the consideration paid and payable is recognised in profit or loss.

# 4. FINANCIAL INSTRUMENTS

## FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES

The Group's major financial instruments include borrowings, trade receivables, bills receivable, trade payables, bills payable and bank balances. Details of these financial instruments are disclosed in respective notes. The risks associated with these financial instruments and the policies on how to mitigate these risks are set out below. The management manages and monitors these exposures to ensure appropriate measures are implemented on a timely and effective manner.

*Fair value interest rate risk*

The Group's fair value interest rate risk relates primarily to fixed-rate borrowings. The Group does not use any derivatives contracts to hedge its exposure to interest rate risk.

The Group currently does not have an interest rate hedging policy. However, the management monitors interest rate exposure and will consider hedging significant interest rate exposure should the need arises.

*Credit risk*

The Group's maximum exposure to credit risk in the event of the counterparties' failure to discharge their obligations as at 31st December, 2006 in relation to each class of recognised financial assets is the carrying amount of those assets as stated in the consolidated balance sheet.

In order to minimise the credit risk, the management of the Group has delegated a team responsible for determination of credit limits, credit approvals and other monitoring procedures to ensure that follow-up action is taken to recover overdue debtors. In addition, the Group reviews the recoverable amount of each individual trade debtor at each balance sheet date to ensure that adequate impairment losses are made for irrecoverable amounts. In this regard, the directors of the Company consider that the Group's credit risk is significantly reduced.

The Group has no significant concentration of credit risk, with exposure spread over a number of counterparties.

The credit risk on liquid funds is limited because the counterparties are banks with high credit ratings assigned by international credit-rating agencies.

## FAIR VALUE

The directors of the Company consider that the carrying amounts of financial assets and financial liabilities recorded at amortised cost in the consolidated financial statements approximate their fair values.

# 5. REVENUE

Revenue represents the amounts received and receivable for goods sold by the Group to outside customers, less sales tax and sales returns during the year.

## 6. SEGMENT INFORMATION

The Group is principally engaged in the production and sale of single-use medical device products and operates in the PRC. All significant identifiable assets of the Group are located in the PRC. Accordingly, no segmental analysis is presented.

## 7. FINANCE COSTS

| | **2006** | 2005 |
|---|---|---|
| | ***RMB'000*** | *RMB'000* |
| Interest on bank borrowings wholly repayable within five years | **21,519** | 17,038 |

## 8. PROFIT BEFORE TAXATION

| | **2006** | 2005 |
|---|---|---|
| | ***RMB'000*** | *RMB'000* |
| Profit before taxation has been arrived at after charging (crediting): | | |
| Allowances for bad and doubtful debts | **5,747** | 3,862 |
| Auditors' remuneration | **1,403** | 830 |
| Depreciation | **43,308** | 23,863 |
| Prepaid lease payments charged to income statement | **1,377** | 1,305 |
| Rental payments in respect of premises under operating leases | **3,240** | 2,831 |
| Research and development expenditure | **8,872** | 8,334 |
| Cost of inventories recognised as an expense | **451,585** | 335,727 |
| Staff costs, including directors' remuneration | | |
| – Retirement benefits scheme contributions (note 28) | **16,058** | 13,184 |
| – Salaries and other allowances | **78,298** | 60,249 |
| Total staff costs | **94,356** | 73,433 |
| Net foreign exchange loss | **220** | 271 |
| Loss on disposals of property, plant and equipment | **54** | 378 |
| Interest income | **(751)** | (589) |
| Rebate of value added tax | **(14,445)** | (13,028) |

*Note:* The Tax Bureau in Weihai agreed to grant a rebate on the value added tax paid by Weihai Jierui Medical Products Company Limited ("Jierui Subsidiary") with effect from 1st May 1999 on the basis of "payment first then rebate". The rebate was granted to Jierui Subsidiary because it was recognised as a "Social Welfare Entity".

## 9. TAXATION

| | **2006** | 2005 |
|---|---|---|
| | ***RMB'000*** | *RMB'000* |
| PRC income tax | **6,745** | 2 |

The Company is recognised as a "High and New Technology Enterprise". In accordance with the "Notice of the State Tax Bureau of the Ministry of Finance Regarding Certain Preferential Treatment Policies on Enterprise Income Tax", the Company was subject to income tax at a tax rate of 15%. Commencing from 1st July 2004, the Company is entitled to an exemption from PRC income tax for the two years starting from its first profit-making year, followed by a 50% tax relief for the next three years. The Company commenced its first profit-making year in 2004. The tax charge provided for the years ended 31st December 2005 and 2006 were made after taking these tax incentives into account.

In accordance with the "Notice of Recognition of Jierui Subsidiary as a Social Welfare Entity" issued by the Civil Administration Bureau of the Shandong Province, Jierui Subsidiary is recognised as a "Social Welfare Entity" and is exempted from PRC income tax.

瀋陽威高金寶商貿有限公司 (Shenyang Weigao Jinbao Trading Co., Limited) ("Weigao Jinbao") is subject to PRC income tax at a tax rate of 33%. Pursuant to the Notice of Ministry of Finance and the State Administration of Taxation concerning certain preferential policies on enterprise income tax ( 財務部 , 國家稅務總局《關於企業所得稅若干優惠政策的通知》) and in accordance with the "Notice of Tax Reduction and Exemption Approval" issued by State Tax Bureau of Shenyang City Shenhe Branch, Weigao Jinbao is exempted from income tax during the year ended 31st December 2005.

山東威高骨科材料有限公司 (Shandong Weigao Orthopaedic Device Company Limited) ("Wego Ortho") is a foreign-invested enterprise operating in the PRC and is entitled to an exemption from PRC income tax for the two years starting from its first profit-marking year, followed by 50% tax relief for the next three years.

Taxation for other PRC subsidiaries are calculated at a tax rate of 33%.

No provision for Hong Kong tax has been made for Weigao International as it did not have assessable profit during the year.

## 9. TAXATION *(Continued)*

The charge for the year can be reconciled to the profit per the consolidated income statement as follows:

| | **2006** | 2005 |
|---|---|---|
| | ***RMB'000*** | *RMB'000* |
| Profit before taxation | **189,348** | 102,580 |
| Taxation at the domestic income tax rate of 33% | **62,485** | 33,851 |
| Tax effect of share of (profit) loss of a jointly controlled entity | **(10,712)** | 479 |
| Tax effect of share of loss of an associate | **—** | 172 |
| PRC income tax exemption | **(33,416)** | (36,205) |
| Tax losses not recognised | **3,338** | 1,258 |
| Tax effect of expenses that are not deductible in determining taxable profit | **1,093** | 447 |
| Effect of differential tax rate on the Company | **(16,043)** | — |
| Taxation | **6,745** | 2 |

At the balance sheet date, the Group has estimated unused tax losses of approximately RMB13,929,000 (2005: RMB3,813,000) available for offset against future profits. No deferred tax asset has been recognised in respect of the tax losses due to the unpredictability of future profit streams. The tax losses can be carried forward for 5 years. Included in unrecognised tax losses are losses of RMB3,813,000 that will expire in 2010, other losses will expire in 2011.

## 10. DIRECTORS', SUPERVISORS' AND EMPLOYEES' EMOLUMENTS

### DIRECTORS' AND SUPERVISORS' EMOLUMENTS

Supervisors are the members of the supervisory committee of the Company.

The emoluments of directors and supervisors during the year are analysed as follows:

| | 2006 | | | | 2005 | | | |
|---|---|---|---|---|---|---|---|---|
| | Fee | Salaries and other allowances | Retirement benefits schemes contributions | Total | Fee | Salaries and other allowances | Retirement benefits schemes contributions | Total |
| | *RMB'000* | *RMB'000* | *RMB'000* | *RMB'000* | *RMB'000* | *RMB'000* | *RMB'000* | *RMB'000* |
| **Executive directors** | | | | | | | | |
| Mr. Zhang Hua Wei | – | 115 | 4 | 119 | – | 104 | 4 | 108 |
| Mr. Miao Yan Guo | – | 91 | 4 | 95 | – | 80 | 4 | 84 |
| Mr. Wang Yi | – | 100 | 4 | 104 | – | 90 | 4 | 94 |
| Mr. Wang Zhi Fan | – | 90 | 4 | 94 | – | 87 | 4 | 91 |
| Mr. Wu Chuan Ming | – | 89 | 4 | 93 | – | 90 | 4 | 94 |
| | – | 485 | 20 | 505 | – | 451 | 20 | 471 |
| **Non-executive directors** | | | | | | | | |
| Mr. Chen Xue Li | – | – | – | – | – | – | – | – |
| Ms. Zhou Shu Hua | – | – | – | – | – | – | – | – |
| | – | – | – | – | – | – | – | – |
| **Independent non-executive directors** | | | | | | | | |
| Mr. Lau Wai Kit | – | – | – | – | 50 | – | – | 50 |
| Mr. Luan Jian Ping | 30 | – | – | 30 | 30 | – | – | 30 |
| Mr. Shi Huan | 30 | – | – | 30 | 30 | – | – | 30 |
| | 60 | – | – | 60 | 110 | – | – | 110 |
| **Supervisors** | | | | | | | | |
| Ms. Bi Hong Mei | – | 87 | 4 | 91 | – | 63 | 3 | 66 |
| Ms. Chen Xiao Yun | – | 63 | 3 | 66 | – | 50 | 3 | 53 |
| Mr. Miao Hai Sheng | – | 73 | 3 | 76 | – | 60 | 4 | 64 |
| | – | 223 | 10 | 233 | – | 173 | 10 | 183 |
| | 60 | 708 | 30 | 798 | 110 | 624 | 30 | 764 |

## 10. DIRECTORS', SUPERVISORS' AND EMPLOYEES' EMOLUMENTS *(Continued)*

### EMPLOYEES' EMOLUMENTS

The five individuals with the highest emoluments for the year ended 31st December, 2005, were all directors of the Company, whilst for the year ended 31st December, 2006, two were directors of the Company, details of whose emoluments are included in the above disclosure.

The emoluments of the remaining three (2005: nil) individuals were as follows:

| | **2006**<br>***RMB'000*** | 2005<br>*RMB'000* |
|---|---|---|
| Salaries and other benefits | **299** | — |
| Retirement benefits schemes contributions | **12** | — |
| | **311** | — |

Their emoluments were within the following band:

| | **2006**<br>**No. of employees** | 2005<br>No. of employees |
|---|---|---|
| Nil to HK$1,000,000 | **3** | — |

During the year ended 31st December, 2006, one of the independent non-executive directors, Mr. Lau Wai Kit, has agreed to waive the directors's fee of approximately RMB 48,000.

During the two years ended 31st December, 2006, no emoluments were paid by the Group to the directors and supervisors as an inducement to join or upon joining the Group or as compensation for loss of office.

## 11. DIVIDENDS

| | **2006** | 2005 |
|---|---|---|
| | ***RMB'000*** | *RMB'000* |
| Dividends recognised as distribution during the year: | | |
| Interim dividend paid, RMB0.02 (2005: RMB0.01) per share | **19,311** | 9,127 |
| Final dividend for 2005 paid, RMB0.02 (2004: RMB0.013) per share | **19,311** | 11,239 |
| | **38,622** | 20,366 |
| Final dividend proposed, RMB0.033 (2005: RMB0.02) per share | **31,863** | 19,311 |

The final dividend of RMB0.033 (2005: RMB0.02) per share has been proposed by the directors and is subject to approval by the shareholders in the forthcoming annual general meeting.

## 12. EARNINGS PER SHARE

The calculation of the basic earnings per share for the year is based on the profit for the year attributable to equity holders of the Company of approximately RMB170,921,000 (2005: RMB101,200,000) and on the 965,560,000 shares (2005: weighted average of 898,957,000 shares) in issue during the year.

No potential ordinary shares were outstanding either in the current or prior year. Diluted earnings per share is not presented.

## 13. PROPERTY, PLANT AND EQUIPMENT

| | Construction in progress | Buildings | Plant and machinery | Motor vehicles | Moulds | Furniture, fixtures and office equipment | Total |
|---|---|---|---|---|---|---|---|
| | *RMB'000* | *RMB'000* | *RMB'000* | *RMB'000* | *RMB'000* | *RMB'000* | *RMB'000* |
| **COST** | | | | | | | |
| At 1st January 2005 | 74,627 | 184,595 | 60,989 | 6,940 | 1,388 | 25,051 | 353,590 |
| Additions | 179,078 | 6,597 | 10,217 | 4,147 | 1,505 | 5,336 | 206,880 |
| Acquisition of subsidiaries | 8,472 | — | 16,510 | 138 | — | 570 | 25,690 |
| Transfer | (228,984) | 132,978 | 93,499 | — | — | 2,507 | — |
| Disposals | — | (6,234) | (700) | (462) | — | (1,909) | (9,305) |
| At 31st December 2005 | 33,193 | 317,936 | 180,515 | 10,763 | 2,893 | 31,555 | 576,855 |
| Additions | 88,292 | 1,414 | 15,375 | 5,446 | 3,574 | 3,755 | 117,856 |
| Transfer | (77,973) | 18,471 | 54,622 | — | 1,874 | 3,006 | — |
| Disposals | — | — | (2,421) | (406) | — | (125) | (2,952) |
| At 31st December 2006 | 43,512 | 337,821 | 248,091 | 15,803 | 8,341 | 38,191 | 691,759 |
| **DEPRECIATION** | | | | | | | |
| At 1st January 2005 | — | 14,102 | 10,531 | 2,280 | 296 | 10,945 | 38,154 |
| Provided for the year | — | 7,166 | 8,303 | 1,600 | 1,122 | 5,672 | 23,863 |
| Eliminated on disposals | — | (1,445) | (491) | (262) | — | (1,212) | (3,410) |
| At 31st December 2005 | — | 19,823 | 18,343 | 3,618 | 1,418 | 15,405 | 58,607 |
| Provided for the year | — | 11,918 | 23,359 | 2,498 | 2,027 | 3,506 | 43,308 |
| Eliminated on disposals | — | — | (1,617) | (386) | — | (66) | (2,069) |
| At 31st December 2006 | — | 31,741 | 40,085 | 5,730 | 3,445 | 18,845 | 99,846 |
| **CARRYING VALUES** | | | | | | | |
| At 31st December 2006 | 43,512 | 306,080 | 208,006 | 10,073 | 4,896 | 19,346 | 591,913 |
| At 31st December 2005 | 33,193 | 298,113 | 162,172 | 7,145 | 1,475 | 16,150 | 518,248 |

## 13. PROPERTY, PLANT AND EQUIPMENT *(Continued)*

The above items of property, plant and equipment other than construction in progress are depreciated on a straight-line basis after taking into account their estimated residual value and at the following rates per annum:

| | |
|---|---|
| Buildings | 3.3% - 10% |
| Plant and machinery | 10% - 20% |
| Motor vehicles | 20% |
| Moulds | 50% |
| Furniture, fixtures and office equipment | 20% |

The buildings of the Group are situated in the PRC and held under medium-term lease.

The construction in progress represented buildings, plant and machinery, moulds and furniture, fixtures and office equipment under construction which are situated in the PRC.

At 31 December 2006, the Group has pledged buildings having a carrying value of approximately RMB194,227,000 (2005: RMB119,029,000) to banks to secure bank loans granted to the Group.

## 14. PREPAID LEASE PAYMENTS

| | **2006** | 2005 |
|---|---|---|
| | ***RMB'000*** | *RMB'000* |
| The Group's prepaid lease payments comprise: | | |
| Leasehold land in PRC | | |
| Medium-term lease | **55,317** | 56,694 |
| Analysed for reporting purposes as: | | |
| Current portion (included in trade and other receivables) | **1,395** | 1,395 |
| Non-current portion | **53,922** | 55,299 |
| | **55,317** | 56,694 |

The leasehold land in PRC are held under medium-term lease of 45-50 years.

At 31 December 2006, the Group has pledged land use rights having a carrying value of approximately RMB43,175,000 (2005: RMB38,102,000) to banks to secure bank loans granted to the Group.

## 15. INTEREST IN A JOINTLY CONTROLLED ENTITY

| | **2006** | 2005 |
|---|---|---|
| | ***RMB'000*** | *RMB'000* |
| Cost of unlisted investment, at cost | **13,000** | 13,000 |
| Share of post-acquisition profit (loss) | **30,805** | (1,657) |
| | **43,805** | 11,343 |

Details of the Group's jointly controlled entity as at 31st December 2006 are as follows:

| **Name** | **Form of business structure** | **Place of incorporation or registration/ operation** | **Attributable equity interest directly held by the Company** | **Principal activities** |
|---|---|---|---|---|
| Shandong JW Medical Products Co., Ltd. | Incorporated | PRC | 50% | Production and sales of medical products |

The summarised financial information in respect of the Group's jointly controlled entity is set out below:

| | **2006** | 2005 |
|---|---|---|
| | ***RMB'000*** | *RMB'000* |
| Total assets | **126,696** | 45,432 |
| Total liabilities | **(39,087)** | (22,746) |
| Net assets | **87,609** | 22,686 |
| Group's share of net assets | **43,805** | 11,343 |
| Revenue | **158,267** | 1,825 |
| Profit (loss) for the year | **64,924** | (2,914) |
| Group's share of profit (loss) of a jointly controlled entity for the year | **32,462** | (1,457) |

## 16. INVENTORIES

| | **2006** | 2005 |
|---|---|---|
| | ***RMB'000*** | *RMB'000* |
| At cost: | | |
| Raw materials | **75,251** | 41,673 |
| Finished goods | **90,934** | 77,696 |
| | **166,185** | 119,369 |

## 17. TRADE AND OTHER RECEIVABLES

The Group allows an average credit period of 90 days to its trade customers. The aging analysis of trade receivables is stated as follows:

| | **2006** | 2005 |
|---|---|---|
| | ***RMB'000*** | *RMB'000* |
| 0 to 90 days | **177,029** | 107,611 |
| 91 to 180 days | **55,073** | 48,192 |
| 181 to 365 days | **39,935** | 26,307 |
| Over 365 days | **10,349** | 7,114 |
| Trade receivables | **282,386** | 189,224 |
| Bills receivable | **3,991** | 1,378 |
| Other receivables, deposits and prepayments | **69,458** | 59,727 |
| | **355,835** | 250,329 |

All the bills receivable are within 90 days.

## 18. PLEDGED BANK DEPOSITS

The amounts represented deposits pledged to banks to secure banking facilities granted to the Group. The amounts had been pledged to secure short-term bank loans and banking facilities and were therefore classified as current assets. The deposits carried fixed interest rate ranging from 0.7% to 2.5% (2005: 0.7% to 2.3%) per annum.

## 19. BANK BALANCES AND CASH

Bank balances and cash comprise cash held by the Group and short-term bank deposits with an original maturity of three months or less. The deposits carried interest rate of 0.7% (2005: 0.7%) per annum.

## 20. TRADE AND OTHER PAYABLES

The aging analysis of trade payables is stated as follows:

| | **2006** | 2005 |
|---|---|---|
| | ***RMB'000*** | *RMB'000* |
| 0 to 90 days | **68,816** | 76,820 |
| 91 to 180 days | **12,242** | 11,386 |
| 181 to 365 days | **5,110** | 2,180 |
| Over 365 days | **2,767** | 4,911 |
| Trade payables | **88,935** | 95,297 |
| Bills payable | **92,750** | 25,820 |
| Other payables and accrued expenses | **72,116** | 25,892 |
| | **253,801** | 147,009 |

All the bills payable will mature within six months.

As at 31st December 2005, the bills payable were under the guarantee provided by the ultimate holding company. During the year ended 31st December 2006, the guarantees provided by the ultimate holding company have been fully released.

## 21. BORROWINGS

| | 2006 | 2005 |
|---|---|---|
| | *RMB'000* | *RMB'000* |
| Secured bank loans | **90,343** | 106,400 |
| Unsecured bank loans | **260,700** | 280,800 |
| Unsecured other loan | **35,000** | — |
| | **386,043** | 387,200 |
| The loans are repayable as follows: | | |
| On demand or within one year | **105,043** | 177,200 |
| More than one year but not exceeding two years | **281,000** | 210,000 |
| | **386,043** | 387,200 |
| Less: Amount due within one year shown under current liabilities | **(105,043)** | (177,200) |
| Amount due after one year | **281,000** | 210,000 |

As at 31st December 2006, the unsecured bank loans of the Group amounting to RMB 260,700,000 (2005: nil) were under the guarantee jointly provided by independent third parties.

As at 31st December 2006, the bank loans of the Group amounting to RMB 343,000 (2005: nil) were secured by bills receivable.

As at 31st December 2005, the unsecured bank loans of the Group amounting to RMB20,000,000 were under the guarantee jointly provided by the ultimate holding company and unrelated companies.

As at 31st December 2005, the unsecured bank loans of the Group amounting to RMB211,500,000 were under the guarantee provided by the ultimate holding company.

The bank loans carried interest ranging from 4.7% to 6.7% (2005: 5.0% to 6.1%) per annum.

## 22. SHARE CAPITAL

| | Nominal value of shares | Number of domestic shares | Number of H shares | Total number of shares | Value |
|---|---|---|---|---|---|
| | *RMB* | | | | *RMB'000* |
| At 1st January 2005 | 0.1 | 600,000,000 | 264,500,000 | 864,500,000 | 86,450 |
| Issue of domestic shares (Note a) | 0.1 | 48,160,000 | — | 48,160,000 | 4,816 |
| Issue of H shares (Note b) | 0.1 | — | 52,900,000 | 52,900,000 | 5,290 |
| At 31st December 2005 and 31st December 2006 | 0.1 | 648,160,000 | 317,400,000 | 965,560,000 | 96,556 |

*Notes:*

(a) Pursuant to an agreement dated 14th March 2005 entered into between Weigao Holding and the Company, the Company agreed to acquire a leasehold land and building under construction in progress for a total consideration of RMB47,000,000 which was satisfied by the issue of 48,160,000 domestic shares of RMB0.1 each in the Company. The transaction was completed on 20th May 2005.

(b) On 30th November 2005, 52,900,000 H shares of RMB0.1 each were issued by the Company at HK$1.35 per share for cash by way of placing. The net proceeds of approximately RMB70,010,000 were used for purchase of production machinery of orthopaedics and blood purification products and as working capital of the Group.

The new shares issued rank pari passu with other shares in issue in all respects.

## 23. ACQUISITIONS OF SUBSIDIARIES

(a) On 17th September, 2005 the Group acquired 95% of the registered capital of 福州帆順醫療器械技術有限公司 ("Fuzhou Fanshun") for a consideration of RMB475,000. This acquisition has been accounted for using the purchase method.

The net assets acquired in the transaction are as follows:

| | **Acquiree's carrying amount before combination and fair value** |
|---|---|
| | *RMB'000* |
| Net assets acquired: | |
| Property, plant and equipment | 164 |
| Inventories | 487 |
| Trade and other receivables | 1,882 |
| Bank and cash balances | 14 |
| Trade and other payables | (2,048) |
| | 499 |
| Minority interests | (24) |
| Total consideration, satisfied by cash | 475 |
| Net cash outflow arising on acquisition: | |
| Cash consideration paid | (475) |
| Cash and cash equivalents acquired | 14 |
| | (461) |

Fuzhou Fanshun contributed approximately RMB711,000 revenue and approximately RMB8,000 loss before taxation to the Group's profit before tax for the period between the date of acquisition and 31st December, 2005.

If the acquisition had been completed on 1st January, 2005, total group revenue for the period would have been RMB572 million, and profit for the period before taxation would have been RMB104 million. The proforma information is for illustrative purposes only and is not necessarily an indication of revenue and results of operations of the Group that actually would have been achieved had the acquisition been completed on 1st January, 2005, nor is it intended to be a projection of future results.

## 23. ACQUISITIONS OF SUBSIDIARIES *(Continued)*

(b) On 29th December, 2005 the Group subscribed an additional 13% of the registered capital of Wego Ortho for a consideration of RMB13,200,000. After the completion of the subscriptions, the Group holds 53% equity interest in Wego Ortho.

The net assets acquired in the transaction are as follows:

| | **Acquiree's carrying amount before combination and fair value** |
|---|---|
| | *RMB'000* |
| Net assets acquired: | |
| Property, plant and equipment | 25,526 |
| Inventories | 15,115 |
| Trade and other receivables | 5,890 |
| Bank and cash balances | 23,550 |
| Trade and other payables | (11,590) |
| Bank borrowings – repayable within one year | (21,864) |
| | 36,627 |
| Minority interests | (15,950) |
| | 20,677 |
| Represented by: | |
| Interest in an associate | 7,477 |
| Cash consideration | 13,200 |
| | 20,677 |
| Net cash inflow arising on acquisition: | |
| Cash consideration paid | (13,200) |
| Bank balances and cash acquired | 23,550 |
| | 10,350 |

## 24. MAJOR NON-CASH TRANSACTION

Pursuant to an agreement dated 14th March, 2005 entered into between Weigao Holding and the Company, the Company agreed to acquire a leasehold land and building under construction in progress for a total consideration of RMB47,000,000 which was satisfied by issue of 48,160,000 domestic shares of RMB0.1 each in the Company.

During the year ended 31st December, 2006, a subsidiary incorporated a new subsidiary with a third party. Plant and machinery with carrying value of RMB7,500,000 was transferred from that third party to the new subsidiary as the consideration of acquiring 48.4% equity interest.

## 25. LEASE COMMITMENTS

### THE GROUP AS LESSEE

At the balance sheet date, the Group had the following future minimum payments under non-cancellable operating leases which fall due as follows:

| | **2006** | 2005 |
|---|---|---|
| | ***RMB'000*** | *RMB'000* |
| Within one year | **2,146** | 834 |
| In the second to fifth year inclusive | **2,299** | 970 |
| Over five years | **1,000** | — |
| | **5,445** | 1,804 |

Operating lease payments represent rentals payable by the Group for its branch office premises, staff quarters and warehouses. Leases are mainly negotiated for a period ranging from two to five years and all rentals are fixed.

### THE GROUP AS LESSOR

Property rental income earned during the year was approximately RMB2,254,000 (2005:RMB 570,000). At the balance sheet date, the Group had contracted with tenants for the following future minimum lease payments.

| | **2006** | 2005 |
|---|---|---|
| | ***RMB'000*** | *RMB'000* |
| Within one year | **2,254** | 1,495 |
| In the second to fifth year inclusive | **1,383** | 2,420 |
| | **3,637** | 3,915 |

Operating lease payments represent rentals receivable by the Group from a portion of its office premises. Leases are negotiated and rentals are fixed for a period ranging from two to five years.

## 26. CAPITAL COMMITMENTS

At 31st December, 2006, the Group had commitments for acquisition of property, plant and equipment which were contracted for but not provided in the consolidated financial statements amounting to approximately RMB31,578,000 (2005: RMB18,189,000).

## 27. RELATED PARTY TRANSACTIONS

(a) Apart from the guarantees from ultimate holding company as disclosed in notes 20 and 21, the Group had the following related party transactions during the two years ended 31st December, 2006:

| | **2006** | 2005 |
|---|---|---|
| | ***RMB'000*** | *RMB'000* |
| Sales to fellow subsidiaries | **3,207** | 981 |
| Purchases from fellow subsidiaries | **759** | 1,183 |
| Rental income from a fellow subsidiary | **1,496** | 570 |
| Purchases from a minority shareholder | **3,298** | — |
| Rental payments to a minority shareholder | **250** | — |
| Purchase of land use rights, property, plant and equipment from ultimate holding company | **—** | 56,000 |
| Purchase of property, plant and equipment from fellow subsidiaries | **—** | 1,034 |
| Rental payments to ultimate holding company | **—** | 162 |
| Rental payments to fellow subsidiaries | **48** | 192 |
| Rental income from a jointly controlled entity | **759** | — |

(b) Compensation of key management personnel

The remuneration of directors and other members of key management during the year was as follows:

| | **2006** | 2005 |
|---|---|---|
| | ***RMB'000*** | *RMB'000* |
| Short-term benefits | **947** | 968 |
| Post-employment benefits | **40** | 42 |
| | **987** | 1,010 |

The remuneration of directors and key executives is determined by the remuneration committee having regard to the performance of individuals and market trends.

## 28. RETIREMENT BENEFITS SCHEMES

The Group operates a mandatory provident fund scheme (the "MPF Scheme") for all qualifying employees of the Group in Hong Kong. The assets of the MPF Scheme are held separately from those of the Group, in funds under the control of the trustees. The contributions are charged to the income statement as incurred.

The Group has established different benefits schemes for its full-time PRC employees according to the relevant PRC regulations and rules, including provision of housing provident fund, medical insurance, retirement insurance, unemployment insurance, labour injury insurance and pregnancy insurance. Pursuant to these existing schemes the Group contributes 8%, 8%, 18%, 2%, 1% and 1% of the basic salary of its employees to the housing provident fund, medical insurance, retirement insurance, unemployment insurance, labour injury insurance and pregnancy insurance, respectively.

The contributions payable to the schemes by the Group are disclosed in note 8.

## 29. POST BALANCE SHEET EVENTS

Subsequent to the balance sheet date, the Group has entered into the following significant transactions:

(1) On 2nd March 2007, the Company entered into an eight-year long-term loan agreement for US$20 million with the International Finance Corporation, a member of the World Bank Group.

(2) On 11th March 2007, the Company, Weigao Holding and Medtronic, Inc. ("Medtronic") have entered into a Non Binding Letter of Intent (the "Letter of Intent") in relation to the proposed investment (the "Proposed Investment") in the Company by Medtronic of up to 15% of the enlarged issued share capital of the Company in form of a combination of existing domestic shares and to be issued new H shares.

## 30. PARTICULARS OF SUBSIDIARIES OF THE COMPANY

Particulars of the Company's subsidiaries as at 31st December, 2006 are as follows:

| Name | Form of business structure | Country of incorporation or registration/ operations | Registered capital | Proportion ownership interest held by the Group Directly | Proportion ownership interest held by the Group Indirectly | Principal activities |
|---|---|---|---|---|---|---|
| 威海潔瑞醫用製品有限公司 (Weihai Jierui Medical Products Co., Limited) | Incorporated | PRC | RMB32,000,000 | 96% | — | Manufacturing of medical PVC granules, plastic packing bags and carton boxes |
| 威海威高血液淨化製品有限公司 (Weihai Weigao Blood Purified Product Co., Limited) | Incorporated | PRC | RMB20,000,000 | 70% | — | Manufacturing of medical blood purification treatments and related consumables |
| 瀋陽威高金寶商貿有限公司 (Shenyang Weigao Jinbao Trading Co., Limited) | Incorporated | PRC | RMB6,000,000 | 90% | — | Trading of medical products |
| 威海威高集團模具有限公司 (Weihai Weigao Group Mould Co., Limited) | Incorporated | PRC | RMB8,000,000 | 90% | 10% | Manufacturing of moulds |
| 山東威高骨科材料有限公司 (Shandong Weigao Orthopedic Device Co., Limited) | Incorporated | PRC | RMB40,000,000 | 53% | — | Manufacturing of medical bond material products |

## 30. PARTICULARS OF SUBSIDIARIES OF THE COMPANY *(Continued)*

| Name | Form of business structure | Country of incorporation or registration/ operations | Registered capital | Proportion ownership interest held by the Group Directly | Proportion ownership interest held by the Group Indirectly | Principal activities |
|---|---|---|---|---|---|---|
| 福州帆順醫療器械技術有限公司 (Fuzhou Fanzhou Medical Device Technology Company Limited) | Incorporated | PRC | RMB500,000 | 95% | — | Trading of medical products |
| 山西威高華鼎醫療器械製造有限公司 (Shanxi Huading Medical Equipment Manufacturing Co., Limited) | Incorporated | PRC | RMB15,500,000 | — | 51.6% | Manufacturing of medical blood purification treatments and related consumables |
| Weigao International Medical Company Limited (威高國際醫療有限公司) | Incorporated | HK | HK$1,000,000 | 100% | — | Trading of medical products |

None of the subsidiaries issued any debt securities at the end of the year or at any time during the year.

# Financial Summary

| | For the year ended 31st December, | | | | |
|---|---|---|---|---|---|
| | **2006** | 2005 | 2004 | 2003 | 2002 |
| | ***RMB'000*** | *RMB'000* | *RMB'000* | *RMB'000* | *RMB'000* |
| **RESULTS** | | | | | |
| Revenue | **786,926** | 569,987 | 407,823 | 317,935 | 278,247 |
| Profit before taxation | **189,348** | 102,580 | 69,867 | 56,802 | 50,727 |
| Taxation | **(6,745)** | (2) | (3,040) | (4,572) | (5,295) |
| Profit for the year | **182,603** | 102,578 | 66,827 | 52,230 | 45,432 |
| Attributable to: | | | | | |
| Equity holders of the Company | **170,921** | 101,200 | 65,888 | 50,454 | 43,526 |
| Minority interests | **11,682** | 1,378 | 939 | 1,776 | 1,906 |
| | **182,603** | 102,578 | 66,827 | 52,230 | 45,432 |

| | As at 31st December, | | | | |
|---|---|---|---|---|---|
| | **2006** | 2005 | 2004 | 2003 | 2002 |
| | ***RMB'000*** | *RMB'000* | *RMB'000* | *RMB'000* | *RMB'000* |
| **ASSETS AND LIABILITIES** | | | | | |
| Total assets | **1,394,119** | 1,132,230 | 735,998 | 517,587 | 344,674 |
| Total liabilities | **(646,273)** | (534,209) | (358,481) | (359,383) | (226,471) |
| Minority interests | **(49,106)** | (31,580) | (8,920) | (2,741) | (4,194) |
| | **698,740** | 566,441 | 368,597 | 155,463 | 114,009 |

NOTICE IS HEREBY GIVEN THAT the Annual General Meeting (the "AGM") of Shandong Weigao Group Medical Polymer Company Limited 山東威高集團醫用高分子製品股份有限公司 (the "Company") will be held at 8:30 a.m. on Wednesday, 9 May 2007 at the registered office of the Company at No. 312 Shichang Road, Weihai City, Shandong Province, PRC for the purpose of considering the following resolutions:

## ORDINARY RESOLUTIONS

1. To consider and approve the audited consolidated financial statements of the Group (including the Company and its subsidiaries) for the year ended 31 December 2006;

2. To consider and approve the report of the board of directors of the Company (the "Board") for the year ended 31 December 2006;

3. To consider and approve the report of the Supervisory Committee of the Company for the year ended 31 December 2006;

4. To consider and approve the profit distribution plan for the year ended 31 December 2006, and the final distribution plan of the Company for the year ended 31 December 2006 and to authorise the Board for the distribution of the final dividends to the shareholders of the Company for the year ended 31 December 2006;

5. To consider and approve the proposal for the re-appointment of Deloitte Touche Tohmatsu as the auditor of the Company for the year ending 31 December 2007, and to authorise the Board to determine its remuneration;

6. To consider and approve the re-appointment of directors of the Company for another term of three years ending 28 February 2010 (The biographical details of directors proposed for reappointment are set out on pages from 34 to 35 of this annual report);

   – To re-elect Mr. Chen Xue Li as non-executive director of the Company

   – To re-elect Mrs. Zhou Shu Hua as non-executive director of the Company

   – To re-elect Mr. Zhang Hua Wei as director of the Company

   – To re-elect Mr. Wang Yi as director of the Company

   – To re-elect Mr. Miao Yan Guo as director of the Company

   – To re-elect Mr. Wang Zhi Fan as director of the Company

   – To re-elect Mr. Wu Chuan Ming as director of the Company

   – To re-elect Mr. Shi Huan as independent non-executive director of the Company

   – To re-elect Mr. Luan Jian Ping as independent non-executive director of the Company

7. To consider and authorise the Board to approve the remuneration of the directors and supervisors of the Company for the year ending 31 December 2007; and

8. To pass the following resolution as a special resolution of the Company;

## SPECIAL RESOLUTION

"THAT:

a) subject to paragraphs (c), (d) and (e) below, the exercise by the Board during the Relevant Period (as herein after defined in paragraph (f)) of all the powers of the Company to allot, issue and deal with Domestic Shares and/or H Shares severally or jointly be and is hereby approved;

b) the approval in paragraph (a) above shall authorise the Board the Relevant Period to make or grant offers, agreement and options which would or might require the exercise of such powers to allot and issue Domestic Shares and/or H Shares during the Relevant Period or after the end of the Relevant Period;

c) the aggregate nominal amount of Domestic Shares allotted and issued or agreed to be allotted and issued (whether pursuant to an option or otherwise) by the board of directors pursuant to paragraphs (a) and (b) above, otherwise than pursuant to (i) Rights Issue (as hereinafter defined in paragraph (f)); (ii) upon the exercise of rights of conversion under the terms of any securities which are convertible into Shares; (iii) upon the exercise of rights of subscription under the terms of any warrants issued by the Company; or (iv) any scrip dividend plan of other similar arrangement in lieu of the whole or part of a dividend on Shares allotted pursuant to the Company's Articles of Association, shall not exceed 20% of the aggregate nominal amount of the Domestic Shares in issue on the date of passing this resolution;

d) the aggregate nominal amount of H Shares allotted and issued or agreed to be allotted and issued (whether pursuant to an option or otherwise) by the board of directors pursuant to paragraphs (a) and (b) above, otherwise than pursuant to (i) Rights Issue (as hereinafter defined in paragraph (f)); (ii) upon the exercise of rights of conversion under the terms of any securities which are convertible into Shares; (iii) upon the exercise of rights of subscription under the terms of any warrants issued by the Company; or (iv) any scrip dividend plan of other similar arrangement in lieu of the whole or part of a dividend on Shares allotted pursuant to the Company's Articles of Association, shall not exceed 20% of the aggregate nominal amount of the H Shares in issue on the date of passing this resolution;

e) the approval referred to in paragraph (a) above is conditional upon the Company obtaining the approval from China Securities Regulatory Commission;

f) for the purpose of this resolution;

"Relevant Period" means the period from the date of the passing of this special resolution until whichever is the earliest of:

i) the conclusion of next annual general meeting of the Company after the passing of this resolution;

ii) the expiration of the period within the twelve month period after the passing of this resolution; or

iii) the revocation or variation of the authority given under this resolution by ordinary resolution of the shareholders of the Company in a general meeting.

"Right Issue" means an offer of shares open for a fixed period to holders of shares on the register of members of the Company and (where appropriate) other holders of the equity securities of the Company that are entitled to accept such offer on a fixed record date in proportion to their then holdings of such shares or such equity securities (subject to such exclusion or other arrangements as the directors of the Company may deem necessary of expedient in relation to fractional entitlements or having regard to any restrictions or obligations under the laws of, or the requirements of, any recognised regulatory body or any stock exchange in relevant jurisdiction); and

g) authorise the Board to, at its discretion, make any amendment of the Articles of Association of the Company where necessary, so as to increase the registered capital of the Company, and to refect the new capital structure upon the granting of approval for the allotment or issue of the shares in the Company pursuant to paragraph (a) above."

By order of the Board
**Shandong Weigao Group Medical Polymer Company Limited**
**Chen Xue Li**
*Chairman*

Weihai, Shandong, the PRC
22 March, 2007

Registered address in the PRC:
No. 312 Shichang Road
Weihai
Shandong
PRC

*As at the date of this report, the board of directors of the Company comprises Mr. Zhang Hua Wei, Mr. Miao Yan Guo, Mr. Wang Yi, Mr. Wang Zhi Fan and Mr. Wu Chuan Ming as the executive directors, Mr. Chen Xue Li and Mrs. Zhou Shu Hua as the non-executive directors, and Mr. Shi Huan, Mr. Luan Jian Ping, Mr. Lau Wai Kit and Mr. Li Jia Miao as the independent non-executive directors.*

*Notes:*

(i) A shareholder who has the right to attend and vote at the AGM is entitled to appoint one proxy (or more) in writing to attend the AGM and vote on his behalf in accordance with the Company's Articles of Association. The proxy need not be a shareholder of the Company. Enclosed herewith a form of proxy for use in the general meeting. In the case of joint registered holders, the proxy from may be signed by any joint registered holder. In the case that any one of such joint registered holders is present at any meeting personally or by proxy, then one of such joint registered holders so present whose name stands first on the register of members of the Company in respect of such share shall alone be entitled to vote in respect thereof.

(ii) To be valid, a form of proxy together with a power of attorney or other authority , if any, under which it is signed or certified by a notary or an official copy of that power of attorney or authority, must be delivered at the Company's H Share Registrars in Hong Kong, Standard Registrars Limited at 26/F, Tesbury Centre, 28 Queen's Road East, Hong Kong (in respect of the H Shareholders of the Company) and the Company's principal place of business at No. 312 Shichang Road, Weihai, Shandong Province, PRC (in respect of domestic Shareholders) not less than 24 hours before the time appointed for holding the AGM or 24 hours before the time designated for voting.

(iii) Shareholders and their proxies attending the AGM shall produce their proof of identification.

(iv) The register of members in Hong Kong will be closed from Tuesday, 10 April 2007 to Wednesday, 9 May 2007, both days inclusive, during which no transfer of shares will be effected. In order to be eligible to attend the AGM and to vote thereat as shareholders, all transfers of shares together with the relevant share certificates must be delivered at the Company's H Share Registrars, Standard Registrars Limited at 26/F, Tesbury Centre, 28 Queen's Road East, Hong Kong no later than 4:00 p.m. on Wednesday, 4 April 2007.

(v) The holders of the Company's H shares who intend to attend the AGM should complete and return the reply slip to the Company's H share Registrars in Hong Kong, Standard Registrars Limited at 26/F, Tesbury Centre, 28 Queen's Road East, Hong Kong no later than Wednesday, 18 April 2007 by hand, by post, by telegraph or by fax to (852) 2528 3158,

(vi) The holders of the Company's Domestic Shares who intend to attend the AGM should complete and return the reply slip to the Company's registered address at No. 312 Shichang Road, Weihai, Shandong Province, PRC no later than Wednesday, 18 April 2007 by hand, by post, by telegraph or by fax to (86) 631 5622419.

(vii) The AGM is expected not to exceed half a day, and all shareholders and proxies shall be responsible for their own traveling and accommodation expenses.

(viii) Pursuant to Article 80 of the Company's Articles of Association, a poll may be demanded by the following persons:

(a) the chairman of the meeting;

(b) at least two shareholders entitle to vote present in person or by proxy;

(c) one or more shareholders present in person or by proxy representing more than 10% of all shares carrying the voting rights at the meeting.

(ix) Any enquiries about this notice and the AGM shall be sent for the attention to Ms. Xing Jingran at No. 312 Shichang Road, Weihai, Shandong Province, PRC (Tel. (86) 631 5622418).