山東羅欣藥業股份有限公司

Shandong Luoxin Pharmacy Stock Co.,Ltd.*

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

Stock Code: 8058

ANNUAL REPORT 2009

* For identification purposes only

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This report, for which the directors (the "Directors") of Shandong Luoxin Pharmacy Stock Co., Ltd. (the "Company") collectively and individually accept full responsibility, 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, (1) the information contained in this report is accurate and complete in all material respects and is not misleading; (2) there are no other matters the omission of which would make any statement in this report misleading; and (3) all opinions expressed in this report have been arrived at after due and careful consideration and are founded on bases and assumptions that are fair and reasonable.

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CORPORATE INFORMATION

DIRECTORS

Executive Directors

Liu Baoqi
Liu Zhenhai
Li Minghua
Han Fengsheng
Chen Yu (appointed on 28 April 2009)

Non-executive Directors

Zhou Wuxian (resigned on 28 April 2009)
Yin Chuangui
Liu Yuxin

Independent non-executive Directors

Foo Tin Chung, Victor
Fu Hongzheng
Li Hongjian

SUPERVISORS

Gao Xiaoling
Sun Song
Zhu Enqiang
Guan Yonghua

COMPLIANCE OFFICER

Liu Baoqi

COMPANY SECRETARY

Lau Hon Kee *(FCPA, CPA(Aust.))*

AUTHORISED REPRESENTATIVES

Liu Baoqi
Lau Hon Kee *(FCPA, CPA(Aust.))*

REGISTERED OFFICE

Luoqi Road, High and New
Technology Experimental Zone, Linyi City
Shandong Province, the PRC

PRINCIPAL PLACE OF BUSINESS IN HONG KONG

Unit 10. 11/F, Tower B
Southmark, 11 Yip Hing Street
Wong Chuk Hang, Hong Kong

MEMBERS OF THE AUDIT COMMITTEE

Foo Tin Chung, Victor *(chairman of the audit committee)*
Fu Hongzheng
Li Hongjian

LEGAL ADVISER TO THE COMPANY

King & Wood
9th Floor, Hutchison House, Central, Hong Kong

AUDITORS

HLB Hodgson Impey Cheng
31/F, Gloucester Tower
The Landmark
11 Pedder St., Central
Hong Kong

H-SHARE SHARE REGISTRAR AND TRANSFER OFFICE

Computershare Hong Kong Investor Services Limited
Rooms 1712-16, 17th Floor
Hopewell Centre
183 Queen's Road East
Hong Kong

PRINCIPAL BANKERS

China Construction Bank
Linyi City Luozhuang District Branch
The Centre of Longtan Road
Luozhuang District, Linyi City
Shandong Province, PRC

Industrial and Commercial Bank of China
Linyi City Luozhuang District Branch
Baoquan Road, Luozhuang District
Linyi City, Shandong Province, PRC

STOCK CODE

8058

CHAIRMAN'S STATEMENT

Dear Shareholders,

On behalf of the board of Directors (the "Board"), it is my pleasure to present the annual report of Shandong Luoxin Pharmacy Stock Co., Ltd. (hereinafter referred to as the "Company") for the year ended 31 December 2009 (hereinafter referred to as the "Year") for your review.

With an aim of maximizing shareholders' value, our Company is devoted to enhancing the capabilities in research and development and consolidating the sales network development. Through dedication and concerted effort of the management and employees, the Company achieved rapid growth and healthy development. For the year ended 31 December 2009, turnover increased by 35.9% to RMB907,453,000, whereas profit attributable to shareholders increased by 46.6% to RMB268,550,000.

In the past year, our capabilities in, among others, management, market network development, technology development, capital operation, elite team building, spiritual civilization development, brand building and goodwill have been improved rapidly, which further enhanced our ability to withstand risks as well as our overall strength. To cope with business development and the ever increasing market demand, the technological renovation of liquid and powder injectables production lines were completed. Among a wide range of new products successfully developed and launched to the market by the Company, some products were granted national invention patents and science and technology progress awards. The Company, having obtained the approval, established the Shandong Lyophilized Powder Injection Pharmaceutical Engineering Technology Research Centre (山東省凍干粉針劑藥物工程技術研究中心), laying a stronger platform for its research and development. The "Luoxin" trademark, after being identified as a "Well-known Trademark in Shandong Province", was recognized by the Trademark Office of the State Administration for Industry and Commerce as a "Famous Trademark in the PRC", while the Company was also accredited as a high and new technology enterprise. All these achievements laid a solid foundation for the Company's rapid growth.

As the Company gained predominance in various aspects, we can thus maintain our rapid and sustainable development. Our advantages include: 1. our remarkable results in successful research and development as well as marketing of state level new medicine; 2. our competitive edge arising from continuous development of new medicine; 3. our experienced management in the pharmaceutical industry; 4. our strength in research and development, and our strong support for research and development as a result of our collaboration with domestic universities and research institutes; 5. our extensive sales and marketing network; 6. our prominent cost advantage achieved by one-stop vertical production ranging from bulk pharmaceutical to finished products.

The Directors believe that the pharmaceutical industry will maintain rapid growth in 2010. Particularly with the acceleration of implementation of medical reform imposed by the State and the proactive introduction of new cooperative medical initiatives, the overal market expenses on medical and pharmaceutical treatment will dramatically increase. Such huge market potential will enable well-established enterprises to enter a new era of rapid development. Moreover, the Ministry of Health has laid down the "Healthy China 2020" (健康中國2020年) plan, which outlined three stages of development: in the first stage, the PRC should establish a systematic sanitary service system covering urban and rural areas by 2010; in the second stage, the PRC should have a top ranking amongst developing countries in terms of sanitary services before 2015; in the third stage, the PRC's sanitary service should maintain a high standard among developing countries by 2020, and is hoped to match the standard of those moderately developed countries. It was also planned that RMB850 billion will be allocated to promote medical services system in the coming three years. If the three-stage plan is implemented as scheduled, the pharmaceutical consumption in the PRC will move into a surging period, which will enable the rapid development of those pharmaceutical enterprises with growth potential.

CHAIRMAN'S STATEMENT

Looking ahead to 2010, the Company has staged into a new horizon and will face new challenges as well as development opportunities. We strongly believe that the Company will be able to maintain faster and better development and achieve unprecedented accomplishments.

The rapid development and advancement of the Company always depends on the sustained effort of the management and employees, as well as the incessant support from all the shareholders, customers, suppliers and business partners. I would like to extend my gratitude to all the Directors for their contribution. I would also like to extend my sincere gratitude on behalf of the Board to all those who have devoted their efforts to facilitate the growth of the Company and have been giving tremendous support for the advancement of the Company.

Liu Baoqi
Chairman
23 March 2010

PROFILES OF DIRECTORS, SUPERVISORS AND SENIOR MANAGEMENT

EXECUTIVE DIRECTORS

Mr. Liu Baoqi (劉保起), aged 48, is an executive Director and the chairman of the Company. He is responsible for the strategic planning and overall management of the Company. Mr. Liu completed his tertiary course in Economics and Management from the School of Shandong Provincial Communist Party (中共山東省委黨校) in 1996. Mr. Liu obtained the qualification of pharmacist. He has about 20 years of experience in the medical and pharmaceutical industry in the PRC. Mr. Liu joined Shandong Luoxin Factory (the predecessor of the Company) in1995. Before joining Shandong Luoxin Factory, Mr. Liu worked for Linyi Luozhuang Pharmacy Company ("Linyi Luozhuang", the predecessor of Luoxin Pharmacy Group Co., Ltd. (Luoxin Pharmacy Group, previously know as Linyi Luoxin Pharmacy Company Limited ("Linyi Luoxin")) from 1988 to 1995. Mr. Liu was named as the Outstanding Young Entrepreneur in Linyi City (臨沂市優秀青年企業家) and one of the Ten Outstanding Young Persons in Linyi City (臨沂市十大傑出青年) in May and October 1996 respectively. Mr. Liu is also a delegate of the Linyi City People's Congress. Mr. Liu is the uncle of Mr. Liu Zhenhai.

Mr. Liu Zhenhai (劉振海), aged 34, is an executive Director and the vice-chairman of the Company. He is responsible for the overall financial and strategic planning of the Company. He has about 14 years of experience in the medical and pharmaceutical industry in the PRC. Before joining the Company in 2001, Mr. Liu Zhenhai had over 7 years' experience working in the accounting and finance department of Linyi Luozhuang. Mr. Liu Zhenhai is also a delegate of the Linyi City People's Congress. Mr. Liu Zhenhai is the nephew of Mr. Liu Baoqi.

Ms. Li Minghua (李明華), aged 44, is an executive Director, the general manager and head of the research and development department of the Company. She is responsible for assisting the chairman of the Company in the Company's overall business development and operation. She graduated from Shenyang Pharmacy University (瀋陽藥科大學) with a bachelor's degree in Pharmacy. Ms. Li is a senior professional engineer in medicine in the PRC certified by Hei Long Jiang Human Resource Department (黑龍江人事廳) and a registered practising pharmacist. Before joining the Company in 2001, Ms. Li had over 15 years' experience working in several pharmaceutical enterprises in the PRC.

Mr. Han Fengsheng (韓風生), aged 34, is an executive Director and the secretary of the Board. Mr. Han graduated from the Dalian University (大連大學) majoring in Computer Science. Before joining the Company in November 2001, Mr. Han had over 5 years' experience working in the information technology department of Linyi Luozhuang Pharmacy Company (the predecessor of Linyi Luoxin).

Mr. Chen Yu (陳雨) ("**Mr. Chen**"), aged 41, was appointed as an executive Director on 28 April 2009 and is the vice general manager of the Company's production department. Mr. Chen completed post-graduate education in Nanjing Chemical Power College (南京化工動力專科學校), and was named a Heat Supply and Ventilation Engineer by Liaoning Province Human Resources Bureau. Mr. Chen has over 28 years of experience in the PRC medicine manufacturing industry.

PROFILES OF DIRECTORS, SUPERVISORS AND SENIOR MANAGEMENT

NON-EXECUTIVE DIRECTORS

Mr. Zhou Wuxian (周武先), aged 52, is a non-executive Director and the legal representative of Qingdao Guofeng Group Jiaozhou Pharmacy Limited ("Qingdao Guofeng Jiaozhou"). Mr. Zhou completed his tertiary course in the Shandong Chinese Medicine College (山東中醫學院). Mr. Zhou has over 24 years' experience in the medical and pharmaceutical industry in the PRC. In November 2004, Mr. Zhou became a non-executive Director of the Company. Mr. Zhou resigned as non-executive directors on 28 April 2009.

Mr. Yin Chuangui (尹傳貴), aged 53, is a non-executive Director, and the authorized representative of Linyi City People's Hospital ("Linyi People Hospital"), a promoter and an initial management shareholder of the Company. Mr. Yin graduated from the Weifang Medical College (濰坊醫學院) with a bachelor's degree specialising in Health Management. In May 2001, Mr. Yin was nominated by Linyi People Hospital as a non-executive Director.

Mr. Liu Yuxin (劉玉欣), aged 51, is a non-executive Director. Mr. Liu completed his tertiary course in the Yishui Medical College (沂水醫學專科學校). In May 2001, Mr. Liu was nominated by Pingyi County People's Hospital ("Pingyi People Hospital"), a promoter and an initial management shareholder of the Company, as a non-executive Director. Mr. Liu is also a member of the Chinese People's Political Consultative Conference of Shandong Province.

INDEPENDENT NON-EXECUTIVE DIRECTORS

Foo Tin Chung Victor (傅天忠), aged 41, has been appointed as an independent non-executive Director since April 2005. Mr. Foo has over 10 years' experience in the finance and accounting fields. Mr. Foo has been the executive director, financial controller, qualified accountant, company secretary and compliance officer of Jinheng Automotive Safety Technology Holdings Limited, a company listed on GEM since June 2004 and transferred to be listed on Main Board in 2008. Mr. Foo was also serving as an independent non-executive director of RBI Holdings Limited, a company listed on the Stock Exchange. Mr. Foo holds a bachelor's degree in Accounting and Information System in the University of New South Wales in Australia and holds a master degree in Business Administration in Australia Graduate School of Management. He is a CPA of the Hong Kong Institute of Certified Public Accountants and a CPA of CPA Australia. Mr. Foo held senior management position in listed companies in Hong Kong and was an auditor of an international audit firm.

Mr. Fu Hongzheng (付宏征), aged 46, was appointed as the independent non-executive Director in June 2001. Mr. Fu graduated from Pharmacy School of Yanbian University (延邊大學藥學院) in 1985 with a bachelors' degree and got his master's degree from the Shenyang Medical University (瀋陽醫科大學) in 1991.

Ms. Li Hongjian (李宏建), aged 56, has been appointed as independent non-executive Director since 30 November 2006. Ms. Li graduated from the Faculty of Pharmacy of Shandong Medical University (山東醫學院藥學系) in 1976. Since her graduation, Ms. Li has been engaging in pharmacy works in hospitals. She is currently the person-in-charge of the pharmacy department and the Chief Pharmacist in Shandong Qian Fo Shan Hospital (山東千佛山醫院), as well as a part-time professor and a mentor to the graduate school students of Shandong University (山東大學).

PROFILES OF DIRECTORS, SUPERVISORS AND SENIOR MANAGEMENT

SUPERVISORS

Ms. Gao Xiaoling (高小玲), aged 46, is the supervisor and the vice general manager of Lijun Group Limited Liability Company ("Lijun Group") (Sales Company), a promoter and an initial management shareholder of the Company. In May 2001, Ms. Gao was nominated by Lijun Group as a member of board of supervisors of the Company.

Mr. Sun Song (孫松), aged 39, is the supervisor and the manager of the Company's bulk medicine workshop. Mr. Sun graduated from the University of Hei Long Jiang (黑龍江大學) in 1993 majoring in Organic Chemistry.

Mr. Zhu Enqiang (祝恩強), aged 46, is the supervisor and the staff representative of the Company. Before joining the Company in 2001, Mr. Zhu had over 9 years' experience working in Linyi Luozhuang.

Mr. Guan Yonghua (管永華), aged 47, is the director and deputy general manger of Linyi Municipal Pharmacy. On 30 November 2007, Mr. Guan was nominated by Linyi Municipal Pharmacy and appointed as supervisor of the Company.

SENIOR MANAGEMENT

Mr. Ji Honghai (季紅海), aged 35, is the vice general manager of the Company and is responsible for the sales and marketing operation of the Company. Mr. Ji graduated from the University of Jinan City Workers (濟南市職工大學) majoring in Financial Accounting. Mr. Ji joined Shandong Luoxin Factory (the predecessor of the Company) in 1997. Mr. Ji joined Shandong Luoxin Factory in 1997. Before joining Shandong Luoxin Factory, he worked for Linyi Luozhuang from 1996 to 1997.

Mr. Zhao Xuekun (趙學昆), aged 74, is the chief engineer of the Company and is responsible for advising the Company's product development, production technology and GMP compliance issues. Mr. Zhao completed his tertiary education in Shenyang Pharmacy College (瀋陽藥學院). Before joining Shandong Luoxin Factory in 1996, Mr. Zhao had over 39 years' experience working in a hospital, drug control and inspection center and the health department of Linyi City.

Mr. Lau Hon Kee (劉漢基), FCPA, CPA (Aust.), aged 39, is the financial controller and company secretary of the Company. Mr. Lau is responsible for accounting, financial reporting and internal control procedures of the Company. Mr. Lau holds a Bachelor's degree in Commerce from Australian National University and Master's degree in Professional Accounting from Hong Kong Polytechnic University. Mr. Lau has also been serving as an independent non-executive director of Strong Petrochemical Holdings Limited since November 2008, a company listed on the Stock Exchange. He is a Fellow CPA of the Hong Kong Institute of Certified Public Accountants and a CPA of CPA Australia. Before joining the Company in March 2003, Mr. Lau has over 10 years' experience in finance & accounting field, and held senior management position in several service and manufacturing companies.

MANAGEMENT DISCUSSION AND ANALYSIS

BUSINESS REVIEW

For the year ended 31 December 2009, the Company remained dedicated to its existing development strategies, continued to strengthen its research and development as well as production and distribution capabilities and maintained a sound operating status. Accordingly, the profit attributable to the shareholders of the Company grew substantially from the corresponding period of last year, achieving strong growth momentum. These achievements were the result of the great support and assistance from all shareholders, customers, suppliers and business partners and the public, as well as the concerted and unremitting efforts of the management team and employees of the Company.

During the year under review, the Company continued to implement effective strategies on its seven major systems covering management, culture, business organization, capital operation, science and technology innovation, human resources and marketing, which effectively boosted the Company's development as well as further enhanced the risk resistance capacity and the overall strength of the Company. Among a wide range of new products successfully developed and launched to the market by the Company, some were granted national invention patents and science and technology progress awards, and more than 20 products were included in the administrative list under the national essential drug list issued by the Ministry of Health of China. The Company is also accredited as a high and new technology enterprise. All these achievements laid a solid foundation for the Company's rapid growth.

Leveraging on its strength, the Company has been awarded the "Top Ten Pharmaceutical Enterprises with Growth Potential" in China and has been one of the "Top 100 Pharmaceutical Companies in China" consecutively since 2006. On the "List of Small and Medium-sized Enterprises in China with Most Potentials" (「中國最具潛力中小企業榜」), the first list published by Forbes in 2010, the Company was selected for three consecutive years and our ranking jumped to the 29th place this year. In April 2009, the "Luoxin" trademark, as a "Well-known Trademark in Shandong Province", was recognized by the Trademark Office of the State Administration for Industry and Commerce as a "Famous Trademark in the PRC", suggesting that the products of the Company are widely acknowledged by the market, and that our brand is recognized by the general public. This is the result of our long-term efforts dedicated to building up our brand, and the demonstration of a growth in our overall corporate strength. By capitalizing on the opportunity arising from this award, we will continue to execute our trademark strategy, upgrade our brand and improve our competitiveness to build the Company into a globally outstanding pharmaceutical brand.

FINANCIAL REVIEW

For the year ended 31 December 2009, the Company's audited turnover was approximately RMB907,453,000, representing an increase of approximately 35.89% from approximately RMB667,792,000 for the corresponding period of last year. The increase was attributable to the Company's launch of products with high added values, upgrade of product portfolio and acceleration of the development of sales network to increase the market share of its products, which boosted an increase in turnover.

For the year ended 31 December 2009, the audited cost of sales was approximately RMB479,736,000, representing an increase of 36.60% from approximately RMB351,196,000 for the corresponding period of last year. The increase in the cost of sales was in line with the increase in turnover.

MANAGEMENT DISCUSSION AND ANALYSIS

For the year ended 31 December 2009, the audited gross profit margin was 47.13%, representing a slight fall of 0.28% from 47.41% for the corresponding period of last year.

For the year ended 31 December 2009, the audited operating expenditure was approximately RMB122,542,000, representing an increase of 56.49% from approximately RMB78,307,000 for the corresponding period of last year.

For the year ended 31 December 2009, the audited profit attributable to the shareholders was approximately RMB268,550,000, representing an increase of 46.62% from approximately RMB183,155,000 for the corresponding period of last year. Weighted average earnings per share were RMB0.441 for the year ended 31 December 2009.

LIQUIDITY AND FINANCIAL RESOURCES

The Company's working capital is generally financed by its internally generated cash flow.

As at 31 December 2009, the Company's cash and cash equivalents amounted to approximately RMB500,943,000 (as at 31 December 2008: RMB145,458,000). As at 31 December 2009, the Company did not have any borrowings (as at 31 December 2008: nil).

PLEDGED BANK DEPOSITS/CASH AND CASH EQUIVALENTS

As at 31 December 2009, the Company's bank deposits amounting to approximately RMB237,194,000 were pledged as security for remittance under acceptance (as at 31 December 2008: bank deposits amounting to approximately RMB14,840,000 were pledged as security for remittance under acceptance).

MAJOR ACQUISITION AND DISPOSAL

For the year ended 31 December 2009, the Company did not have any major acquisition or disposal.

SIGNIFICANT INVESTMENT

For the year ended 31 December 2009, the Company did not make any significant investment.

CONTINGENT LIABILITIES

As at 31 December 2009, the Company did not have any substantial contingent liabilities.

MANAGEMENT DISCUSSION AND ANALYSIS

EXCHANGE RISK

The Company operates and conducts business in the PRC, and all the Company's transactions, assets and liabilities are denominated in RMB.

Most of the Company's cash and cash equivalents and pledged deposits are denominated in RMB, while bank deposits are placed with banks in the PRC. Any remittance from the PRC is subject to the restrictions on foreign exchange control imposed by the PRC government.

EMPLOYEES AND REMUNERATION POLICY

The Directors believe that employees' quality is the most important factor in maintaining the sustained development and growth of the Company and in raising its profitability. The Company determines its employees' salaries based on their performance, work experience and the prevailing salaries in the market, while other remuneration and fringe benefits are maintained at an appropriate level.

The Company has established a remuneration committee to make recommendations on the overall strategy for remuneration policy.

PROSPECTS

With the growing emphasis China has placed on the development of the pharmaceutical industry and the healthcare protection benefits for its citizens, coupled with the approval by the State Council in April 2009 of "The Opinion Concerning Further Reform on Medical and Sanitary Systems" (《關於深化醫療衛生體制改革的意見》) and "The Latest Implementation Emphasis Scheme for the Pharmaceutical and Sanitary Systems Reform (2009-2011)" (《醫藥衛生體制改革近期重點實施方案(2009-2011)》), governments at all levels in the PRC are expected to commit RMB850 billion in the next three years in order to accelerate and promote the establishment of a primary healthcare protection scheme. This is anticipated to bring more business opportunities to the pharmaceutical industry. The management of the Company is therefore confident in the prospects of the pharmaceutical industry.

Looking ahead, with the commitment to the strategic guiding theory of becoming a "Technology-driven enterprise with determination and efforts", the Company will fully capitalize on the opportunities arising from the consolidation of the pharmaceutical industry by continuing to focus on product research and development and enhancing the capability of its research and development team, and by accelerating the build-up of sales team to establish a more extensive sales network for increasing the market share of its products. In addition, the Company also aims at reducing production costs and accelerating the expansion of production and sales, so as to build up its strength in terms of scale, low cost and differential competition. Following the launch of products with higher added values, the management of the Company is confident that the Company is able to maintain a steady business growth and generate satisfactory returns for its shareholders.

MANAGEMENT DISCUSSION AND ANALYSIS

AUDIT COMMITTEE

The Company has established an audit committee (the "Audit Committee") with written terms of reference in compliance with paragraph C3 of the Code Corporate Governance Practices (the "Code") as set out in Appendix 15 of the GEM Listing Rules. The duties of the Audit Committee are to review and supervise the financial reporting process and the Company's internal control policies and procedures. The appointments of the Audit Committee members are based on their broad experience in the medicinal field and professional knowledge in financial reporting and management.

The Audit Committee meets regularly to review the financial reporting matters and internal control policies and procedures issues; and see how the Company can comply with these requirements. The Audit Committee also acts as the communication bridge between the Board and the auditors in relation to the planning and scope of audit work. The audited results of the Company for the year have been reviewed by the Audit Committee.

CORPORATE GOVERNANCE

The Board considers that good corporate governance of the Company is the key to safeguarding the interests of the shareholders and enhancing the performance of the Company. The Board is committed to maintain and ensure high standard of corporate governance and will continuously review and improve the corporate governance practices and standards of the Company to ensure that business activities and decision making process are regulated in a proper and prudent manner.

During the year, the Company has complied with all the code provisions of the Code.

PURCHASE, SALE OR REDEMPTION OF LISTED SECURITIES

The Company has not redeemed any of its listed securities during the year. The Company has not purchased or sold any of the Company's listed securities during the year.

CLOSURE OF REGISTER OF MEMBERS

The registers of members of the Company will be closed from 7 May 2010 to 7 June 2010 (both days inclusive). All properly completed H Shares transfer forms accompanied by the relevant share certificates must be lodged with the Register of H Shares in Hong Kong, Computershare Hong Kong Investor Services Limited at Shops 1712 -16, 17th Floor, Hopewell Centre, 183 Queen's Road East, Wanchai, Hong Kong, no later than 4:30 pm on 6 May 2010, for registration.

MANAGEMENT DISCUSSION AND ANALYSIS

WITHHOLDING OF CORPORATE INCOME TAX FOR NON-RESIDENT CORPORATE SHAREHOLDERS IN RESPECT OF THE PROPOSED 2009 FINAL DIVIDEND

Pursuant to the Law on Corporate Income Tax of the PRC and the relevant implementing regulations, which came into force on 1 January 2008, the Company is required to withhold corporate income tax at the rate of 10% before distributing the final dividend to non-resident enterprise shareholders whose names appear on the H share register of members on 7 May 2010. Any H shares registered in the name of non-individual shareholders, including HKSCC Nominees Limited, other nominees, trustees or other groups and organizations will be treated as being held by non-resident enterprise shareholders and the Company will distribute the final dividend to such non-individual shareholders after withholding a 10% corporate income tax. The 10% corporate income tax will not be withheld from the final dividend payable to any natural person shareholders whose names appear on the H share register of members of the Company on 7 May 2010. Any natural person investor whose H shares are registered under the name of any such non-individual shareholders and who does not wish any corporate income tax be withheld by the Company may consider transferring the legal title of the relevant H shares into his or her name and duly lodge all transfer documents together with the relevant H share certificates with the Company's H share registrar for registration. In order to determine the list of holders of H shares who are entitled to receive the final dividend, the H share register of members of the Company will be closed from 7 May 2010 to 7 June 2010, both days inclusive, during which period no transfer of the Company's H shares will be effected. In order for holders of H shares to be qualified for the final dividend, all transfer documents accompanied by the relevant share certificates must be lodged with the Company's H share registrar in Hong Kong, Computershare Hong Kong Investors Services Limited, at Shops 1712-1716, 17th Floor, Hopewell Centre, 183 Queen's Road East, Wanchai, Hong Kong, no later than 4:30 p.m. on 6 May 2010, for registration.

The Company will strictly comply with the relevant PRC tax laws and regulations to withhold for payment such appropriate corporate income tax and the final dividend will only be payable to the shareholders whose names appear on the Company's H share register of members on 7 May 2010. The Company will have no liability in respect of any claims arising from any delay in, or inaccurate determination, of the status of the shareholders or any disputes over the mechanism of withholding.

By order of the Board
Shandong Luoxin Pharmacy Stock Co., Ltd*
Liu Baoqi
Chairman

PRC, 23 March 2010

CORPORATE GOVERNANCE REPORT

Pursuant to Rules 18.44 of the GEM Listing Rules, the Board presents this corporate governance report to disclose its corporate governance practices adopted during the year to the shareholders. This report highlights some of the most important corporate governance practices of the Company.

The Board considers that good corporate governance of the Company is the key to safeguarding the interests of the shareholders and enhancing the performance of the Company. The Board is committed to maintain and ensure high standard of corporate governance and will continuously review and improve the corporate governance practices and standards of the Company to ensure that business activities and decision making process are regulated in a proper and prudent manner. During the year, the Company has complied with all the code provisions of the Code on Corporate Governance Practices (the "Code") contained in Appendix 15 of the GEM Listing Rules.

THE BOARD

The Board currently comprises of 5 executive Directors (4 executive Directors prior to 28 April 2009), namely, Mr. Liu Baoqi, Mr. Liu Zhenhai, Ms. Li Minghua, Mr. Han Fengsheng and Mr. Chen (appointed on 28 April 2009) with Mr. Liu Baoqi acting as chairman of the Board, currently 2 non-executive Directors (3 non-executive Directors prior to 28 April 2009), namely, Mr. Zhou Wuxian (resigned on 28 April 2009), Mr. Yin Chuangui and Mr. Liu Yuxin and 3 independent non-executive Directors, namely, Mr. Foo Tin Chung, Victor, Mr. Fu Hongzheng and Ms. Li Hongjian. As the Company was established in the PRC, 4 supervisors namely, Ms. Gao Xiaoling, Mr. Sun Song, Mr. Zhu Enqiang and Mr. Guan Yonghua were also appointed to monitor the decision making of the Board.

Biographical details of the Directors and supervisors and their respective relationships (if any) have been set out in the section "Profiles of Directors, supervisors and senior management" in this report.

In accordance with Article 96 of the articles of association of the Company (the "Articles of Association"), the current term of the Directors (including non-executive Directors but excluding Mr. Chen) is for a period of 3 years running from 30 November 2007, the date on which the above Directors were duly re-elected and appointed

The Board is responsible for the overall strategic development and operation of the Company. The Board is also responsible for the financial performance and internal control policies and procedures of the Company's business operation.

CORPORATE GOVERNANCE REPORT

COMMITMENTS

The full Board will meet every quarter, to review the overall development, operation and financial performance of such period and other matters of the Company that require the approval of the Board. All Board members are given access to board materials and are given reasonable time to review information and sufficient time for consideration. The chairman of the Board is responsible for preparing the agenda of the Board meetings.

Moreover, the Board meets regularly to discuss the daily operation issues of the Company. For those non-executive and independent non-executive Directors who are not personally present at such Board meetings, conference call will be arranged so as to enable the Company to take advice actively from them.

APPOINTMENT OF DIRECTORS

The Directors all carried out their duties in a dedicated, diligent and proactive manner with reasonable prudence. They carried our their duties imposed by the Company Law, Companies Ordinances, the Articles of Association and the GEM Listing Rules, complied with relevant requirements and strictly implemented resolutions passed at general meetings.

Executive directors were appointed based on their expertise and are responsible for different areas of the Company's business. The non-executive Directors and supervisors were mostly appointed through the nominations made by certain initial management shareholders, promoters or staff union, who could monitor the decision making of the Board and operation of the Company.

Two of the promoters, Linyi People's Hospital and Pingyi People Hospital, sold their shares in the Company to independent investors and Linyi Luoxin during October 2007. But as they played a role in the Company's performance and transactions in 2008 and 2009, and will continue to play their role in subsequent events in 2010, the non-executive directors nominated by them will remain on the Board until further arrangement.

The independent non-executive directors also serve important role in the Board. They bring independent judgment on issues of strategic direction and future development; opine on connected transactions and risk management on audit issues. One of the independent non-executive Directors is a qualified accountant and the rest of them possess the qualification set out in GEM Listing Rules as at the date of this report. The Board has received annual confirmation in respect of the independence of each of the independent non-executive Directors and believes that their independence is in compliance with the GEM Listing Rules as at the date of this report.

The Board will consider the past performance, qualification, general market conditions and the Articles of Association in selecting and recommending candidates for Directorships. All Directors are regularly updated on governance and regulatory matters and are entitled to have access to independent professional advice pursuant to the internal policies of the Company.

CORPORATE GOVERNANCE REPORT

BOARD MEETINGS

During year 2009, the Board has held 4 meetings. Directors were given sufficient time to review documents and information relating to matters discussed during such meetings.

Details of Directors' attendance at Board meetings held in 2009 are as follows:

	Dates of meeting			
Board Meetings	**5 March**	**11 May**	**3 August**	**10 November**
Executive Directors				
Mr. Liu Baoqi	✓	✓	✓	✓
Mr. Liu Zhenhai	✓	✓	✓	✓
Ms. Li Minghua	✓	✓	✓	✓
Mr. Han Fengsheng	✓	✓	✓	✓
Mr. Chen Yu (appointed on 28 April 2009)			✓	✓
Non-executive Directors				
Mr. Zhou Wuxian (resigned on 28 April 2009)	✓	✓		
Mr. Yin Chuangui	✓	✓	✓	✓
Mr. Liu Yuxin	✓	✓	✓	✓
Independent non-executive Directors				
Mr. Foo Tin Chung, Victor	✓	✓	✓	✓
Mr. Fu Hongzheng	✓	✓	✓	✓
Ms. Li Hongjian	✓	✓	✓	✓

DIRECTORS' SECURITIES TRANSACTIONS

The Company has adopted a model code of conduct for securities dealings by Directors on terms no less exacting than the required standard of dealings as set out in Rules 5.48 to 5.67 of the GEM Listing Rules. The Company has confirmed, after making specific enquiries with the Directors, the Directors have complied with the required standard of dealings and such code of conduct in relation to securities dealings by Directors for the year ended 31 December 2009.

CHAIRMAN AND CHIEF EXECUTIVE OFFICER

Under A.2.1 of the Code, "the roles of chairman and chief executive officer should be separated and should not be performed by the same individual". During the year ended 31 December 2009, Mr. Liu Baoqi served as chairman of the Board and Ms. Li Minghua served as the General Manager and chief executive officer of the Company.

CORPORATE GOVERNANCE REPORT

COMMITTEES

As part of the corporate governance practices, the Board has established the following committees which are all chaired and comprise independent non-executive directors.

AUDIT COMMITTEE

The audit committee of the Company ("Audit Committee") was established on 20 November 2005 and its current members during the year ended 31 December 2009 include:

Mr. Foo Tin Chung, Victor *(Chairman)*
Mr. Fu Hongzheng
Ms. Li Hongjian

The Company has established an audit committee (the "Audit Committee") with written terms of reference in compliance with paragraph C3 of the Code. The duties of the Audit Committee are to review and supervise the financial reporting process and the Company's internal control policies and procedures. The appointments of the Audit Committee members are based on their broad experience in the medicinal field and professional knowledge of financial reporting and management.

The Audit Committee meets regularly to review the financial reporting matters and internal control policies and procedures issues; and see how the Company can comply with these requirements. The Audit Committee also acts as the communication bridge between the Board and the auditors in relation to the planning and scope of audit work. The audited results of the Company for the year have been reviewed by the Audit Committee.

During the year ended 31 December 2009, the Audit Committee has held four meetings and details of attendances of the meeting are shown below:

	Dates of meeting			
Audit Committee Meetings	**4 March**	**8 May**	**4 August**	**9 November**
Independent non-executive Directors				
Mr. Foo Tin Chung, Victor	✓	✓	✓	✓
Mr. Fu Hongzheng	✓	✓	✓	✓
Ms. Li Hongjian	✓	✓	✓	✓

CORPORATE GOVERNANCE REPORT

REMUNERATION COMMITTEE

The remuneration committee of the Company ("Remuneration Committee") was established in December 2005 and its members during the year ended 31 December 2009 include:

Mr. Foo Tin Chung, Victor *(Chairman)*
Mr. Fu Hongzheng
Ms. Li Hongjian

The Company established the Remuneration Committee with written terms of reference in compliance with paragraph B1 of the Code. The duties of the Remuneration Committee include the evaluation of the performance and making recommendations on the remuneration package of the Directors and senior management and the evaluation and making of recommendations on other employee benefit arrangements.

The appointments of the Remuneration Committee members are based on their broad experience in the medicinal field and knowledge of financial management, in particular, the remuneration to local workforces, as Mr. Fu Hongzheng and Ms. Li Hongjian are both experienced medical professional in the PRC.

During the year ended 31 December 2009, the Remuneration Committee has held four meetings and details of the attendances of the meeting are shown below:

	Dates of meeting			
Remuneration Committee Meetings	**4 March**	**8 May**	**4 August**	**9 November**
Independent non-executive Directors				
Mr. Foo Tin Chung, Victor	✓	✓	✓	✓
Mr. Fu Hongzheng	✓	✓	✓	✓
Ms. Li Hongjian	✓	✓	✓	✓

INVESTOR RELATIONSHIP AND COMMUNICATION

The Company is committed to a policy of open and regular communication and reasonable disclosure of information to its shareholders and public investors. Information of the Company is disseminated to the shareholders and interested parties in the following manner:

* delivery of the quarterly, interim and annual results and reports to all shareholders and interest parties;

* publication of announcements on the quarterly, interim and annual results on the Stock Exchange websites, and issue of other announcements and shareholders' circulars in accordance with the continuing disclosure obligation under the GEM Listing Rules;

CORPORATE GOVERNANCE REPORT

The Company has appointed the IR division of Quam (H.K.) Limited as the Company's investor relationship service provider. All of the Company's investor relationship information could be found on:

http://quamir.com/quamir/ircompanydetail.action?cold=1128&islr=y

ACCOUNTABILITY AND AUDIT

The Directors are responsible for overseeing the preparation of accounts of each financial period by the management. The Directors are also committed to make appropriate announcement, in accordance with GEM Listing Rules, to disclose all information that is necessary for shareholders to assess the financial performance and other matters of the Company.

During the year ended 31 December 2009, the Board has reviewed the engagement of auditors and their remuneration. The auditor of the Company would receive approximately HK$480,000 for audit and related service and approximately HK$208,000 for other services.

INTERNAL CONTROL

The Board is also responsible for reviewing the internal control policies of the Company regularly. Senior management members are required to work in accordance with the internal policies and procedures implemented by the Company. The Company has developed and established an Internal Control Policies and Procedures prior to the listing of the H Shares of the Company on GEM in December 2005. This set of policies and procedures monitors the operation of the Company in three areas, namely: sales and accounts receivables cycles, purchase and accounts payables cycles, and other policies and procedures, including statutory and regulatory reporting and disclosure requirements. Emphasis has been placed on the level of approval on the utilization of the Company's resources and compliance with financial reporting and disclosure requirements. The Audit Committee will also give advice on internal control issues and take an active role in communicating with the Directors and senior management for the best practice of internal control of the Company.

The Company will keep on reviewing the policies and procedures in order to maintain high level of internal control of its operation.

REPORT OF THE DIRECTORS

The Board is pleased to present the report of the Directors for the year ended 31 December 2009 (the "year").

PRINCIPAL ACTIVITIES AND GEOGRAPHICAL ANALYSIS OF OPERATIONS

The principal activity of the Company and the Group is the manufacture and sale of pharmaceutical products.

RESULTS AND DIVIDENDS

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

The directors recommend the payment of a final dividend of RMB0.02 per ordinary share, totalling RMB12,192,000. Such recommendation is subject to the approval of the shareholders of the Company at the forthcoming annual general meeting of the Company.

CLOSURE OF REGISTER OF MEMBERS

The registers of members of the Company will be closed from 7 May 2010 to 7 June 2010 (both days inclusive). All properly completed H Shares transfer forms accompanied by the relevant share certificates must be lodged with the Register of H Shares in Hong Kong, Computershare Hong Kong Investor Services Limited at Shop 1712-16, 17th Floor, Hopewell Centre, 183 Queen's Road East, Wanchai, Hong Kong, no later than 4:30 p.m. on 6 May 2010, for registration.

RESERVES

Movements in the reserves of the Company during the year are set out in Note 33 to the accounts.

PROPERTY, PLANT AND EQUIPMENT

Details of the movements in property, plant and equipment of the Group and the Company are set out in Note 20 to the accounts.

SHARE CAPITAL

Details of the movements in share capital of the Company are set out in Note 32 to the accounts.

DISTRIBUTABLE RESERVES

According to the Company Law of the People's Republic of China, the distributable reserves of the Company at 31 December 2009, amounted to RMB619,961,000 (2008: RMB363,603,000).

REPORT OF THE DIRECTORS

FIVE YEARS FINANCIAL SUMMARY

A summary of the results and of the assets and liabilities of the Group for the last five financial years is set out on page 93 of this report.

COMPARISON BETWEEN BUSINESS OBJECTIVE AND ACTUAL BUSINESS PROGRESS

The business objectives stated in the prospectus which remain still outstanding and not yet fulfill are the commencement of promotional activities for and production of Rhodiola for Injection.

The promotional activities for Rhodiola for Injection, including press release and other target customer oriented promotional activities, has not yet officially commenced as the Company has not obtained the production approval. But the patent in respect of Rhodiola for Injection has been obtained by the Company on 10 May 2006 which was widely reported.

The production of Rhodiola for Injection has not yet commenced either and the Company is in the process of obtaining the production approval from PRC Government.

PURCHASE, SALE OR REDEMPTION OF LISTED SECURITIES

The Company has not redeemed any of its listed securities during the year. The Company has not purchased or sold any of the Company's listed securities during the year.

SHARE OPTIONS

The Company did not adopt any share option plan since its establishment.

Directors
The directors during the year were:

Executive directors
Liu, Baoqi (劉保起)
Liu, Zhenhai (劉振海)
Li, Minghua (李明華)
Han, Fengsheng (韓風生)
Chen, Yu (陳雨) (appointed on 28 April 2009)

REPORT OF THE DIRECTORS

Non-executive directors
Liu, Yuxin (劉玉欣)
Yin, Chuangui (尹傳貴)
Zhou, Wuxian (周武先) (resigned on 28 April 2009)

Independent non-executive directors
Fu, Hongzheng (付宏征)
Foo, Victor Tin Chung (傅天忠)
Li Hongjian (李宏健)

In accordance with Article 96 of the Articles of Association adopted by the shareholders of the Company on 20 November 2005, the term of directorship for most of the Director is for a term of three years running from 30 November 2004, being the date of the general meeting of the Company which approved the appointments of the Directors. The last term of the directors' service was expired and was re-elected as follows:

Mr. Liu, Baoqi (劉保起), Mr. Liu, Zhenhai (劉振海), Ms. Li, Minghua (李明華) being executive Directors, retired and were re-elected on 30 November 2007.

Mr. Han Fengsheng (韓風生), an executive Director, was appointed on 30 November 2006. Mr. Han entered into a service agreement with the Company for a term of three years commencing from 30 November 2006, subject to the retirement and re-election requirements of the Articles of Association at the next annual general meeting of the Company. Mr. Han retired and was re-elected on 30 November 2007.

Mr. Chen Yu (陳雨), an executive Director, was appointed on 28 April 2009. Mr. Chen entered into a service agreement with the Company for a term of three years commencing from 28 April 2009, subject to the retirement and re-election requirements of the Articles of Association, in line with other directors' three years' term of service, at the coming shareholders meeting to be held in November 2010.

Mr. Liu, Yuxin (劉玉欣), Mr. Yin, Chuangui (尹傳貴), Mr. Zhou, Wuxian (周武先), non-executive Directors, retired and were re-elected on 30 November 2007. Mr. Zhou resigned on 28 April 2009.

Mr. Fu, Hongzheng (付宏征), an independent non-executive Director, retired and was re-elected on 30 November 2007.

Mr. Foo, Victor Tin Chung (傅天忠), an independent non-executive Director, was appointed on 8 April 2005. Mr. Foo retired and was re-elected on 30 November 2007.

Ms. Li Hongjian (李宏建), an independent non-executive Director, was appointed on 30 November 2006. Ms. Li entered into a service agreement with the Company for a term of three years commencing from 30 November 2006, subject to the retirement and re-election requirements of the Articles of Association at the next annual general meeting of the Company. Ms. Li retired and was re-elected on 30 November 2007.

REPORT OF THE DIRECTORS

DIRECTORS' SERVICE CONTARCTS

Each of the executive Directors, non-executives Directors, independent non-executive Directors and supervisors of the Company has entered into a service contract with the Company commencing from various dates of their respective appointments for a term of three years.

Save as disclosed above, none of the Directors and supervisors of the Company has entered into service contracts with Company which were not terminable by the Company within one year without compensation (other than statutory compensation).

DIRECTORS AND SUPERVISORS' IN INTEREST IN CONTRACTS

Save as disclosed above, none of the Directors and supervisors of the Company had a material interest, either directly or indirectly, in any contracts of significance in relation to the Company's business during the year.

DIRECTORS' AND SUPERVISORS' INTERESTS IN THE SHARES, UNDERLYING SHARES AND DEBENTURES OF THE COMPANY

As at 31 December 2009, the interests and short positions of each Directors and supervisors of the Company in the shares, underlying shares and debentures of the Company, as recorded in the register required to be kept by the Company under Section 352 of Part XV of the Securities and Futures Ordinance (the "SFO"), or as otherwise notified to the Company and the Stock Exchange pursuant to Rule 5.46 of the GEM Listing Rules were as follows:

Long position of domestic shares of the Company ("Domestic Sahres"), as at 31 December 2009

Name of director	Capacity/ Nature of Interest	Number of domestic shares	% of total issued domestic shares	% of Company's Share Capital
Mr. Liu Baoqi (劉保起) *(Note 1)*	Interest of controlled corporation	238,639,949	53.62%	39.15%
Mr. Liu Zhenhai (劉振海)	Beneficial Owner	35,000,000	7.86%	5.74%

Note

1: These 238,639,949 Domestic Shares are registered in the name of Luoxin Pharmacy Group Co, Ltd ("Luoxin Pharmacy Group", previously know as Linyi Luoxin Pharmacy Company Limited). Liu Baoqi (劉保起) ("Mr. Liu") is interested in 51.72% of the registered share capital of Luoxin Pharmacy Group. Mr. Liu is entitled to exercise or control the exercise of one-third or more of the voting power at the general meeting of Luoxin Pharmacy Group. For the purpose of the SFO, Mr. Liu is deemed to be interested in the entire 238,639,949 Domestic Shares held by Luoxin Pharmacy Group. The total number of Domestic Shares deemed to be interested by Mr. Liu as at 31 December 2009 was 238,639,949 (representing 53.62% of total issued Domestic Shares and 39.15% of Company's share capital).

REPORT OF THE DIRECTORS

SUBSTANTIAL SHAREHOLDERS' INTERESTS AND/OR SHORT POSITION IN THE SHARES, UNDERLYING SHARES OF THE COMPANY

In respect of the register of substantial shareholders (not being a Director or supervisor of the Company) required to be kept under section 336 of Part XV of the SFO shows that as at 31 December 2009, the Company had been notified of the following substantial shareholders' interests and short positions, being 5% or more of the Company's issued share capital. These interests are in addition to those disclosed above in respect of the Directors and supervisors of the Company.

Long position of domestic shares of the Company, as at 31 December 2009

Name	Capacity/ Nature of Interest	Number of domestic shares	% of total issued domestic shares	% of Company's Share Capital
Luoxin Pharmacy Group	Beneficial Owner	238,639,949	53.62%	39.15%
Zuo Hongmei (左洪梅)	Family interest *(note 1)*	238,639,949	53.62%	39.15%
Cao Tingting (曹婷婷)	Family interest *(notes 2, 4)*	35,000,000	7.86%	5.74%
Liu Zhendong (劉振東)	Beneficial Owner *(note 4)*	35,000,000	7.86%	5.74%
Chen Weiwei (陳偉偉)	Family interest *(notes 3, 4)*	35,000,000	7.86%	5.74%

Notes:

1. These 238,639,949 Domestic Shares are registered in the name of Luoxin Pharmacy Group. Luoxin Pharmacy Group is owned as to approximately 51.72% by Mr. Liu. As Mr. Liu is entitled to exercise or control the exercise of one-third or more of the voting power at the general meeting of Luoxin Pharmacy Group, for the purpose of the SFO, Mr. Liu is deemed to be interested in the entire 238,639,949 Domestic Shares held by Luoxin Pharmacy Group. Zuo Hongmei (左洪梅), as wife of Mr. Liu, is taken to be interested in the entire 238,639,949 Domestic Shares held by Mr. Liu.

2. These 35,000,000 Domestic Shares are registered in the name of Liu Zhenhai (劉振海) ("Mr. ZH Liu"). For the purpose of the SFO, Cao Tingting (曹婷婷), as wife of Mr. ZH Liu, is taken to be interested in the entire 35,000,000 Domestic Shares held by Mr. ZH Liu.

3. These 35,000,000 Domestic Shares are registered in the name of Liu Zhendong (劉振東) ("Mr. ZD Liu"). For the purpose of the SFO, Chen Weiwei (陳偉偉), as wife of Mr. ZD Liu, is taken to be interested in the entire 35,000,000 Domestic Shares held by Mr. ZD Liu.

4. Each of Cao Tingting, Mr. ZD Liu, Chen Weiwei, are not considered to be a substantial shareholder for the purpose of the GEM Listing Rules as each of them is less than 10% of the total registered share capital of the Company.

REPORT OF THE DIRECTORS

CONTRACTS OF SIGNIFICANCE

During the year, the Company did not enter into any significant contract. However, a framework agreement of continuing connected transaction, entered into with Luoxin Pharmacy Group, the controlling shareholder of the Company in 2007 which remained effective during the year. Please refer to the section on Connected Transactions and Continuing Connected Transactions for details.

MANAGEMENT CONTRACTS

No contracts concerning the management and administration of the whole or any substantial part of the business of the Company were entered into or existed during the year.

MAJOR SUPPLIERS AND CUSTOMERS

The percentages of purchases and sales for the year attributable to the Company's major suppliers and customers are as follows:

Purchases	
– the largest supplier	12.1%
– five largest suppliers combined	38.5%
Sales	
– the largest customer	13.2%
– five largest customers combined	21.7%

During the year ended 31 December 2009, the sales of chemical medicines to Luoxin Pharmacy Group, Linyi People Hospital and Pinyi People Hospital amounted to approximately RMB119,688,000, RMB15,671,000 and RMB98,000 respectively. Luoxin Pharmacy Group is the largest customer of the Company for the year ended 31 December 2009.

REPORT OF THE DIRECTORS

CONNECTED TRANSACTIONS AND CONTINUING CONNECTED TRANSACTIONS

During the year ended 31 December 2009, the Company had the following non-exempt continuing connected tractions, details of which are set out below:

		Annual Cap for the financial years ending 31 December		
	Nature of transaction	**2007**	**2008**	**2009**
(a)	Sales of chemical medicines from the Company to Luoxin Pharmacy Group pursuant to a framework agreement on 16 September 2007	RMB20 million	RMB85 million	RMB120 million
(b)	Sales of chemical medicines from the Company to Pinyi People Hospital pursuant to a framework agreement on 16 September 2007	RMB4 million	RMB16 million	RMB22 million
(c)	Sales of chemical medicines by the Company to Pinyi People Hospital pursuant to a framework agreement dated 16 September 2007	RMB1.5 million	RMB6 million	RMB8 million

Luoxin Pharmacy Group is the single largest and a substantial shareholder of the Company. Linyi People Hospital and Pinyi People Hospital are promoters of the Company. They are therefore connected persons of the Company pursuant to Rule 20.11 of the GEM Listing Rules. The sale of the chemical medicines from the Company to Luoxin Pharmacy Group, Linyi People Hospital and Pinyi People Hospital pursuant to the respective framework agreements constitute continuing connected transactions of the Company, details of which are set our in an announcement and a circular issued by the Company on 16 September 2007 and 6 October 2007 respectively.

REPORT OF THE DIRECTORS

During the year ended 31 December 2009, the sales of chemical medicines by the Company to Luoxin Pharmacy Group, Linyi People Hospital and Pinyi People Hospital amounted to RMB119,688,000, RMB15,671,000 and RMB98,000 (2008: RMB56,890,000, RMB13,610,000, RMB1,319,000) respectively which did not exceed the annual cap for the relevant transactions. Further details are set out in Note 37 to the consolidated financial statements. The Company received confirmation from auditors that these transactions are complied with the matters stated in Rule 20.38 of the GEM Listing Rules.

The independent non-executive Directors, who are not interested in any of the above continuing connected transactions, have reviewed and confirmed that the above continuing connected transactions have been entered into by the Company:–

(a) in the ordinary and usual course of the business of the Company;

(b) on terms no less favourable to the Company than terms available from independent third parties; and

(c) in accordance with the relevant agreement governing them on terms that are fair and reasonable and in the interest of the shareholders of the Company as a whole.

The Directors have received a letter from the auditors in respect of the continuing connected transactions as required by Rule 20.38 of the GEM Listing Rules.

SUFFICIENCY OF PUBLIC FLOAT

Based on information that is publicly available to the Company and within the knowledge of the Directors, at least 25% of the Company's total issued share capital was held by the public as at the date of this report.

COMPETING BUSINESS

Set out below is information disclosed pursuant to paragraph 11.04 of GEM Listing Rules:–

Luoxin Pharmacy Group

Luoxin Pharmacy Group is the controlling shareholder of the Company which holds 39.15% of the Company's issued share capital. The chairman of the Company Mr. Liu Baoqi is also an executive director and chairman of Luoxin Pharmacy Group and a controlling shareholder holding 51.72% of the registered capital of Luoxin Pharmacy Group.

REPORT OF THE DIRECTORS

Before a non-competition undertaking in favour of the Company was signed by Luoxin Pharmacy Group on 7 November 2002, Luoxin Pharmacy Group was engaged in the sales of chemical medicines, Chinese medicines, medical equipment, health and beauty products. Since the execution of the non-competition undertaking, Luoxin Pharmacy Group has ceased its chemical medicine business. In June 2005, Luoxin Pharmacy Group signed a supplementary non-competition undertaking whereby it will carry out its sales activities in Linyi City only and confirmed that its customers are small and mid-sized medical institutions which are hospitals below county-level. The Company had received from Luoxin Pharmacy Group an annual confirmation in respect of the compliance of these undertakings.

Linyi Municipal Pharmacy Group Company ("Linyi Municipal Pharmacy")

Linyi Municipal Pharmacy is a State-owned enterprise established in the PRC, holding approximately 1.42% of the registered share capital of the Company. Linyi Municipal Pharmacy is principally engaged in the sale of Chinese and chemical medicines, medical equipment and health products in Linyi City and nearby districts. To the best knowledge of the Directors, Linyi Municipal Pharmacy is not and will not engage in the development and manufacturing of medicine products and it has no research and development and production capabilities for medicine manufacturing in the PRC.

Linyi Municipal Pharmacy serves as a regional distributor in Linyi city and nearby districts, and procures medicine products from other suppliers in the PRC. The Directors advised that some of medicine products sold by Linyi Municipal Pharmacy having the same or similar curative effects with those of the Company may be in competition with the products of the Company.

Save as disclosed above, none of the Directors, the substantial shareholders of the Company or their respective associate (as defined in the GEM listing Rules) had any interests in a business which competes or is likely to compete, either directly or indirectly, with the business of the Company.

AUDITORS

The accounts have been audited by HLB Hodgson Impey Cheng who will retire and, being eligible, will offer themselves for re-appointment at the forthcoming annual general meeting.

On behalf of the Board
Liu Baoqi
Chairman

Hong Kong, 23 March 2010

INDEPENDENT AUDITORS' REPORT

HLB 國衛會計師事務所
Hodgson Impey Cheng

Chartered Accountants
Certified Public Accountants

31/F, Gloucester Tower
The Landmark
11 Pedder Street
Central
Hong Kong

TO THE SHAREHOLDERS OF SHANDONG LUOXIN PHARMACY STOCK CO., LTD.
(incorporated in the People's Republic of China with limited liability)

We have audited the consolidated financial statements of Shandong Luoxin Pharmacy Stock Co., Ltd. (the "Company") and its subsidiary (collectively referred to as the "Group") set out on pages 31 to 92 which comprise the consolidated statement of financial position as at 31 December 2009, and the consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows 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.

AUDITORS' 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.

INDEPENDENT AUDITORS' REPORT

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 auditors' judgement, 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 auditors consider 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 31 December 2009 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.

HLB Hodgson Impey Cheng
Chartered Accountants
Certified Public Accountants

Hong Kong, 23 March 2010

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

For the year ended 31 December 2009

	Notes	2009 RMB'000	2008 RMB'000
Turnover	7	**907,453**	667,792
Cost of sales		**(479,736)**	(351,196)
Gross profit		**427,717**	316,596
Other revenue	7	**3,767**	2,613
Other income	9	**2,501**	2,894
Selling and distribution expenses		**(79,668)**	(48,869)
General and administrative expenses		**(42,874)**	(29,438)
Share of profit of an associate	17	**4,063**	3,107
Finance costs	8	**(240)**	(1,250)
Profit before taxation	9	**315,266**	245,653
Taxation	10	**(46,716)**	(62,498)
Profit for the year		**268,550**	183,155
Other comprehensive income for the year, net of tax		**–**	–
Total comprehensive income for the year		**268,550**	183,155
Profit attributable to:			
Owners of the Company		**268,550**	183,155
Minority interests		**–**	–
		268,550	183,155
Total comprehensive income attributable to:			
Owners of the Company		**268,550**	183,155
Minority interests		**–**	–
		268,550	183,155
Earnings per share attributable to owners of the Company (RMB)	15		
– Basic and diluted		**0.441**	0.300

All of the Group's operations are classed as continuing.

The accompanying notes form an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

As at 31 December 2009

	Notes	2009 RMB'000	2008 RMB'000
Non-current assets			
Interest in an associate	17	26,790	22,727
Purchased technical know-how	18	1,996	2,690
Prepayments to acquire technical know-how	19	7,520	10,100
Property, plant and equipment	20	260,221	250,898
Construction-in-progress	21	9,293	–
Prepaid lease payments	22	10,901	11,175
Deferred tax assets	23	2,103	1,682
Goodwill	24	165	–
		318,989	299,272
Current assets			
Inventories	25	246,604	131,278
Trade and bills receivables	26	66,188	68,202
Other receivables, deposits and prepayments	27	87,749	37,512
Pledged bank deposits	28	237,194	14,840
Cash and bank balances	28	263,749	130,618
		901,484	382,450
Current liabilities			
Trade and bills payables	29	328,995	65,854
Other payables and accruals	30	92,294	87,648
Deposits received		9,042	8,194
Taxation payable		13,593	7,431
Dividend payable		7,314	–
		451,238	169,127
Net current assets		450,246	213,323
Total asset less current liabilities		769,235	512,595
Non-current liability			
Deferred income	31	20,380	20,380
Net assets		748,855	492,215

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

As at 31 December 2009

	Notes	2009 RMB'000	2008 RMB'000
Capital and reserves			
Share capital	32	**60,960**	60,960
Other reserves		**67,652**	67,652
Retained earnings			
– Proposed final dividend		**12,192**	12,192
– Others		**607,769**	351,411
Equity attributable to owners of the Company		**748,573**	492,215
Minority interests		**282**	–
Total equity		**748,855**	492,215

Approved by the Board of Directors on 23 March 2010 and signed on its behalf by:

Liu Baoqi
Director

Liu Zhenhai
Director

The accompanying notes form an integral part of these consolidated financial statements.

STATEMENT OF FINANCIAL POSITION

As at 31 December 2009

	Notes	2009 RMB'000	2008 RMB'000
Non-current assets			
Interest in a subsidiary	16	459	-
Interest in an associate	17	26,790	22,727
Purchased technical know-how	18	1,996	2,690
Prepayments to acquire technical know-how	19	7,520	10,100
Property, plant and equipment	20	260,216	250,898
Construction-in-progress	21	9,293	-
Prepaid lease payments	22	10,901	11,175
Deferred tax assets	23	2,103	1,682
		319,278	299,272
Current assets			
Inventories	25	246,604	131,278
Trade and bills receivables	26	66,188	68,202
Other receivables, deposits and prepayments	27	87,209	37,512
Pledged bank deposits	28	237,194	14,840
Cash and bank balances	28	263,718	130,618
		900,913	382,450
Current liabilities			
Trade and bills payables	29	328,995	65,854
Other payables and accruals	30	92,294	87,648
Deposits received		9,042	8,194
Taxation payable		13,593	7,431
Dividend payable		7,314	-
		451,238	169,127
Net current assets		449,675	213,323
Total asset less current liabilities		768,953	512,595
Non-current liability			
Deferred income	31	20,380	20,380
Net assets		748,573	492,215

STATEMENT OF FINANCIAL POSITION

As at 31 December 2009

	Notes	2009 RMB'000	2008 RMB'000
Capital and reserves			
Share capital	32	**60,960**	60,960
Other reserves		**67,652**	67,652
Retained earnings			
– Proposed final dividend		**12,192**	12,192
– Others		**607,769**	351,411
Total equity		**748,573**	492,215

Approved by the Board of Directors on 23 March 2010 and signed on its behalf by:

Liu Baoqi
Director

Liu Zhenhai
Director

The accompanying notes form an integral part of these financial statements.

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

For the year ended 31 December 2009

	Share capital RMB'000	Share premium RMB'000	Statutory surplus reserve fund RMB'000 (Note 33(i))	Statutory public welfare fund RMB'000 (Note 33(ii))	Retained earnings RMB'000	Attributable to owners of the Company RMB'000	Minority interests RMB'000	Total RMB'000
At 1 January 2008	60,960	31,139	30,303	6,033	192,817	321,252	–	321,252
Total comprehensive income for the year	–	–	–	–	183,155	183,155	–	183,155
Transfer from retained earnings to statutory surplus reserve fund	–	–	177	–	(177)	–	–	–
Dividend paid	–	–	–	–	(12,192)	(12,192)	–	(12,192)
At 31 December 2008 and 1 January 2009	60,960	31,139	30,480	6,033	363,603	492,215	–	492,215
Total comprehensive income for the year	–	–	–	–	268,550	268,550	–	268,550
Dividend paid	–	–	–	–	(12,192)	(12,192)	–	(12,192)
Minority interests arising on the acquisition of a subsidiary (Note 34)	–	–	–	–	–	–	282	282
At 31 December 2009	**60,960**	**31,139**	**30,480**	**6,033**	**619,961**	**748,573**	**282**	**748,855**

	Retained earnings RMB'000
Representing:	
Proposed 2009 final dividends	12,192
Others	607,769
Retained earnings as at 31 December 2009	619,961

The accompanying notes form an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF CASH FLOWS

For the year ended 31 December 2009

	Notes	2009 RMB'000	2008 RMB'000
Cash flows from operating activities			
Profit before taxation		315,266	245,653
Adjustments for:			
Interest income		(2,191)	(842)
Interest expense		240	1,250
Share of profit of an associate	17	(4,063)	(395)
Excess of acquirer's share of the net fair value of the associate's identifiable assets, liabilities and contingent liabilities over cost	17	-	(2,712)
Reversal of obsolete inventories written down	25	(878)	(354)
Reversal of impairment loss recognised in respect of trade receivables	26	(266)	(215)
Reversal of impairment loss recognised in respect of other receivables	27	(217)	(45)
Depreciation of property, plant and equipment	20	17,203	13,030
(Gain)/loss on disposal of property, plant and equipment		(167)	283
Write-down of obsolete inventories	25	1,377	879
Impairment loss recognised in respect of prepayments to acquire technical know-how	19	2,430	170
Impairment loss recognised in respect of trade receivables	26	1,861	535
Impairment loss recognised in respect of other receivables	27	541	433
Amortisation of prepaid lease payments	22	274	273
Amortisation of purchased technical know-how	18	844	935
Operating profit before working capital changes		332,254	258,878
Increase in inventories		(115,825)	(62,697)
Decrease/(increase) in trade and bills receivables		419	(14,623)
Increase in other receivables, deposits and prepayments		(50,020)	(29,298)
Increase in trade and bills payables		263,140	33,679
Increase in deposits received		848	731
Increase in other payables and accruals		8,684	39,127

CONSOLIDATED STATEMENT OF CASH FLOWS

For the year ended 31 December 2009

	Notes	2009 RMB'000	2008 RMB'000
Cash generated from operations		**439,500**	225,797
Interest received		**2,191**	842
Interest paid		**(240)**	(1,250)
PRC income tax paid		**(40,975)**	(65,242)
Net cash inflow from operating activities		**400,476**	160,147
Cash flows from investing activities			
Acquisition of an associate		**-**	(19,620)
Acquisition of a subsidiary	34	**(428)**	-
Purchase of property, plant and equipment		**(13,018)**	(10,953)
Additions of construction-in-progress		**(27,971)**	(59,566)
Proceeds from disposal of property, plant and equipment		**1,304**	1,919
Net cash outflow from investing activities		**(40,113)**	(88,220)
Cash flows from financing activities			
Dividend paid		**(4,878)**	(12,192)
New bank loans		**-**	60,000
Repayment of bank loans		**-**	(90,500)
Increase in pledged bank deposits		**(222,354)**	(14,840)
Net cash outflow from financing activities		**(227,232)**	(57,532)
Net increase in cash and cash equivalents		**133,131**	14,395
Cash and cash equivalents at the beginning of year		**130,618**	116,223
Cash and cash equivalents at the end of year		**263,749**	130,618
Analysis of the balances of cash and cash equivalents			
Cash and bank balances		**263,749**	130,618

The accompanying notes form an integral part of these consolidated financial statements.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2009

1. GENERAL INFORMATION

The Company was established as a collectively-owned enterprise under the name of Shandong Luoxin Factory in the People's Republic of China (the "PRC") on 14 December 1995 and was converted into a joint stock co-operative enterprise on 12 July 1997. On 19 November 2001, Shandong Luoxin Factory underwent a corporate reorganisation and was transformed into a joint stock limited liability company by way of promotion with a registered capital of Renminbi ("RMB") 46,000,000. Subsequent to the above reorganisation, the name of the Company was changed to Shandong Luoxin Pharmacy Stock Co., Ltd. The H shares of the Company have been listed on the Growth Enterprise Market ("GEM") of the Stock Exchange of Hong Kong Limited (the "Stock Exchange") since 9 December 2005.

The Company's registered office is located at Luoqi Road, High and New Technology Experimental Zone, Linyi City, Shandong Province, the PRC.

The principal activities of the Company are manufacturing and sales of pharmaceutical products.

The consolidated financial statements are presented in RMB and all values are rounded to the nearest thousand (RMB'000), unless otherwise stated.

These consolidated financial statements were approved for issue by the Board on 23 March 2010.

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

In the current year, the Group has applied all of the new and revised standards, amendments and interpretations ("new HKFRSs") issued by the Hong Kong Institute of Certified Public Accountants (the "HKICPA") that are relevant to its operations and effective for annual periods beginning on or after 1 January 2009.

HKFRSs (Amendments)	Improvements to HKFRSs issued in 2008, except for the amendment to HKFRS 5 that is effective for annual periods beginning or after 1 July 2009
HKFRSs (Amendments)	Improvements to HKFRSs issued in 2009 in relation to the amendment to paragraph 80 of HKAS 39
HKAS 1 (Revised)	Presentation of Financial Statements
HKAS 23 (Revised)	Borrowing Costs
HKAS 32 & 1 (Amendments)	Puttable Financial Instruments and Obligations Arising on Liquidation
HKFRS 1 & HKAS 27 (Amendments)	Cost of an Investment in a Subsidiary, Jointly Controlled Entity or Associate
HKFRS 2 (Amendment)	Vesting Conditions and Cancellations
HKFRS 7 (Amendment)	Financial Instruments: Disclosures – Improving Disclosures about Financial Instruments
HKFRS 8	Operating Segments

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2009

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

HK(IFRIC) – Int 9 & HKAS 39 (Amendments)	Embedded Derivatives
HK(IFRIC) – Int 13	Customer Loyalty Programmes
HK(IFRIC) – Int 15	Agreements for the Construction of Real Estate
HK(IFRIC) – Int 16	Hedges of a Net Investment in a Foreign Operation
HK(IFRIC) – Int 18	Transfers of Assets from Customers

The impact of the application of the above new HKFRSs is discussed below.

HKAS 1 (Revised) affects certain disclosures of financial statements. Under the revised standard, the Income Statement, the Balance Sheet and the Cash Flow Statement are renamed as the "Statement of Comprehensive Income", the "Statement of Financial Position" and the "Statement of Cash Flows" respectively. All income and expenses arising from transaction with non-owners are presented under the "Statement of Comprehensive Income"; while the owners' changes in equity are presented in the "Statement of Changes in Equity". This change in presentation has no effect on reported profit or loss, total income and expense or net assets for any period presented.

HKFRS 8 is a disclosure standard that has resulted in a redesignation of the Group's reportable segments (see Note 6).

The amendments to HKFRS 7 expand the disclosures required in relation to fair value measurements and liquidity risk. The Group has not presented comparative information for the expanded disclosures in accordance with the transitional provision set out in the amendments.

Except for those as disclosed above, the Directors anticipate that the application of these new HKFRSs has no material impact on the results and the financial position of the Group.

The Group has not applied in advance the following new and revised HKFRSs that have been issued but are not yet effective.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2009

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

HKFRSs (Amendments)	Amendments to HKFRS 5 as part of Improvements to HKFRSs issued in 2008[1]
HKFRSs (Amendments)	Improvements to HKFRSs issued in 2009[2]
HKAS 24 (Revised)	Related Party Disclosures[6]
HKAS 27 (Revised)	Consolidated and Separate Financial Statements[1]
HKAS 28 (Revised)	Investments in Associates[1]
HKAS 32 (Amendment)	Classification of Right Issues[4]
HKAS 39 (Amendment)	Eligible Hedged Items[1]
HKFRS 1 (Amendment)	Limited Exemption from Comparative HKFRS 7 Disclosures for First-time Adopters[5]
HKFRS 2 (Amendment)	Group Cash-settled Share-based Payment Transactions[3]
HKFRS 3 (Revised)	Business Combinations[1]
HKFRS 9	Financial Instruments (relating to the classification and measurement of financial assets)[7]
HK(IFRIC) – Int 14 (Amendments)	Prepayments of a Minimum Funding Requirements[6]
HK(IFRIC) – Int 17	Distributions of Non-cash Assets to Owners[1]
HK(IFRIC) – Int 19	Extinguishing Financial Liabilities with Equity Instruments[5]

[1] Effective for annual periods beginning on or after 1 July 2009

[2] Effective for annual periods beginning on or after 1 July 2009 and 1 January 2010, as appropriate

[3] Effective for annual periods beginning on or after 1 January 2010

[4] Effective for annual periods beginning on or after 1 February 2010

[5] Effective for annual periods beginning on or after 1 July 2010

[6] Effective for annual periods beginning on or after 1 January 2010

[7] Effective for annual periods beginning on or after 1 January 2013

HKFRS 9 *Financial Instruments* introduces new requirements for the classification and measurement of financial assets and will be effective from 1 January 2013, with earlier application permitted. The standard requires all recognised financial assets that are within the scope of HKAS 39 *Financial Instruments: Recognition and Measurement* to be measured at either amortised cost or fair value. Specifically, debt investments that (i) are held within a business model whose objective is to collect the contractual cash flows and (ii) have contractual cash flows that are solely payments of principal and interest on the principal outstanding are generally measured at amortised cost. All other debt investments and equity investments are measured at fair value. The application of HKFRS 9 might affect the classification and measurement of the Group's financial assets.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2009

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

In addition, as part of *Improvements to HKFRSs* issued in 2009, HKAS 17 *Leases* has been amended in relation to the classification of leasehold land. The amendments will be effective from 1 January 2010, with earlier application permitted. Before the amendments to HKAS 17, leasees were required to classify leasehold land as operating leases and presented as prepaid lease payments in the consolidated statement of financial position. The amendments have removed such a requirement. Instead, the amendments require the classification of leasehold land to be based on the general principles set out in HKAS 17, that are based on the extent to which risks and rewards incidental to ownership of a leased asset lie with the lessor or the lessee. The application of the amendments to HKAS 17 might affect the classification and measurement of the Group's leasehold land.

The Directors anticipate that the application of the other new and revised HKFRSs will have no material impact on the financial performance and the financial position of the Group.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The consolidated financial statements have been prepared in accordance with HKFRSs (which also include Hong Kong Accounting Standards ("HKASs") and interpretations) issued by the HKICPA, accounting principles generally accepted in Hong Kong, the disclosure requirements of the Hong Kong Companies Ordinance and the applicable disclosure provisions of The Rules Governing the Listing of Securities on GEM of the Stock Exchange (the "GEM Listing Rules").

The preparation of consolidated financial statements in conformity with HKFRSs requires management to make judgements, estimates and assumptions that affect the application of policies and reported amounts of assets, liabilities, income and expenses. The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making judgements about carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates. The estimates and assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimates is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods.

Judgements made by management in the application of HKFRSs that have significant effect on the consolidated financial statements and estimates with a significant risk of material adjustments in the next year are discussed in Note 4 to the consolidated financial statements.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2009

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Basis of preparation

The consolidated financial statements have been prepared on the historical cost basis except for certain financial assets and financial liabilities, which are measured at fair values, as explained in the accounting policies set out below.

Basis of consolidation

The consolidated financial statements included the financial statements of the Company and entities (including special purpose entities) controlled by the Company (its subsidiary). 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 statement of comprehensive income 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 subsidiary to bring their accounting policies in 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 subsidiary 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.

Business combinations

The acquisition of businesses 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 that meet the conditions for recognition under HKFRS 3 *Business Combinations* are recognised at their fair values at the acquisition date, except for non-current assets (or disposal groups) that are classified as held for sale in accordance with HKFRS 5 *Non-current Assets Held for Sale and Discontinued Operations*, which are recognised and measured at fair value less costs to sell.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2009

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Business combinations (Continued)

Goodwill arising on acquisition is recognised as an asset and initially measured at cost, being the excess of the cost of the business combination over the Group's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities recognised. If, after reassessment, the Group's interest in the net fair value of the acquiree's identifiable assets, liabilities and contingent liabilities exceeds the cost of the business combination, the excess is recognised immediately in profit or loss.

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.

Goodwill

Goodwill arising on an acquisition of a business represents the excess of the cost of acquisition over the Group's interest in the fair value of the identifiable assets, liabilities and contingent liabilities of the relevant business at the date of the acquisition. Such goodwill is carried at cost less any accumulated impairment losses.

Goodwill arising on an acquisition of a business is presented separately in the consolidated statement of financial position.

For the purposes of impairment testing, goodwill arising from an acquisition is allocated to each of the relevant cash-generating units, or groups of cash-generating units, that are expected to benefit from the synergies of the acquisition. A cash-generating unit to which goodwill has been allocated is tested for impairment annually, and whenever there is an indication that the unit may be impaired. For goodwill arising on an acquisition in a financial year, the cash-generating unit to which goodwill has been allocated is tested for impairment before the end of that financial year. When the recoverable amount of the cash-generating unit is less than the carrying amount of the unit, the impairment loss is allocated to reduce the carrying amount of any goodwill allocated to the unit first, and then to the other assets of the unit pro rata on the basis of the carrying amount of each asset in the unit. Any impairment loss for goodwill is recognised directly in the consolidated statement of comprehensive income. An impairment loss for goodwill is not reversed in subsequent periods.

On subsequent disposal of the relevant cash-generating unit, the attributable amount of goodwill capitalised is included in the determination of the amount of profit or loss on disposal.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2009

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Investment in an associate

An associate is an entity over which the Group has significant influence and that is neither a subsidiary nor an interest in a joint venture. Significant influence is the power to participate in the financial and operating policy decisions of the investee but is not control or joint control over those policies.

The results and assets and liabilities of an associate are incorporated in these consolidated financial statements using the equity method of accounting. Under the equity method, investment in an associate is initially recognised in the consolidated statement of financial position at cost and adjusted thereafter for the post-acquisition changes in the Group's share of the net assets of the associate, less any impairment in the value of individual investments. When the Group's share of losses of an associate exceeds the Group's interest in that associate (which includes any long-term interests that, in substance, form part of the Group's net investment in the associate), the Group discontinues recognising its share of further losses. Additional losses are provided only to the extent that the Group has incurred legal or constructive obligations or made payments on behalf of the associate.

Any excess of the cost of acquisition over the Group's share of the net fair value of the identifiable assets, liabilities and contingent liabilities of the associate recognised at the date of acquisition is recognised as goodwill. The goodwill is included within the carrying amount of the investment and is not tested for impairment separately. Instead, the entire carrying amount of the investment is tested for impairment as a single asset. Any impairment loss recognised is not allocated to any asset, including goodwill, that forms part of the carrying amount of the investment in the associate. Any reversal of impairment loss is recognised to the extent that the recoverable amount of the investment subsequently increases.

Any excess of the Group's share of the net fair value of the identifiable assets, liabilities and contingent liabilities over the cost of acquisition, after reassessment, is recognised immediately in profit or loss.

Where a group entity transacts with the associate of the Group, profits and losses are eliminated to the extent of the Group's interest in the relevant associate.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2009

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Property, plant and equipment

Property, plant and equipment are stated at historical cost less accumulated depreciation and any accumulated impairment losses. Historical cost includes expenditure that is directly attributable to the acquisition of the items.

Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. All other repairs and maintenance are expensed in profit or loss during the period in which they are incurred.

Depreciation of property, plant and equipment is calculated using the straight-line method to allocate cost to their residual values over their estimated useful lives, as follows:

Buildings	20 – 40 years
Plant and machinery	10 years
Motor vehicles	5 years
Office equipment	5 years

The asset's residual values and useful lives are reviewed, and adjusted if appropriate, at the end of each reporting period.

An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount (see Note 4).

Gains and losses on disposals are determined by comparing proceeds with carrying amount.

Construction-in-progress

Construction-in-progress comprises buildings, plant and machinery on which construction work or installation has not been completed and which, upon completion, management intends to use for long-term purpose. It is stated at cost which includes construction expenditure incurred, interest on loan and other direct costs attributable to the construction or installation less any accumulated impairment losses. On completion, the buildings, plant and machinery are transferred to respective categories at cost less any accumulated impairment losses.

Leasehold land

Interest in leasehold land is accounted for as operating leases and amortised over the lease term on a straight-line basis.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2009

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Purchased technical know-how

Purchased technical know-how is stated at cost less accumulated amortisation and any accumulated impairment losses. It is recognised as an intangible asset if it is probable that the future economic benefits that are attributable to the asset will flow to the Group and amortised on a straight-line basis over its estimated economic life of a period of five years since the commencement of related production.

Impairment of non-financial assets

At the end of the reporting period, the Group reviews the carrying amounts of its tangible and intangible assets to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss, if any. In addition, intangible assets with indefinite useful lives and intangible assets not yet available for use are tested for impairment annually, and whenever there is indication that they may be impaired.

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, unless the relevant asset is carried at a revalued amount under another standard, in which case the impairment loss is treated as a revaluation decrease under that standard.

Where an impairment loss subsequently reverses, the carrying amount of the asset is increased to the revised estimate of its recoverable amount, but so 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 immediately in profit or loss, unless the relevant asset is carried at a revalued amount under another standard, in which case the reversal of the impairment loss is treated as a revaluation increase under that standard.

Financial instruments

Financial assets and financial liabilities are recognised when a group entity becomes a party to the contractual provisions of the instrument. Financial assets and financial liabilities are initially measured at fair value. Transaction costs that are directly attributable to the acquisition or issue of financial assets and financial liabilities (other than financial assets and financial liabilities at fair value through profit or loss) are added to or deducted from the fair value of the financial assets or financial liabilities, as appropriate, on initial recognition. Transaction costs directly attributable to the acquisition of financial assets or financial liabilities at fair value through profit or loss are recognised immediately in profit or loss.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2009

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Financial instruments (Continued)

Financial assets

The Group's financial assets are classified into loans and receivables. All regular way purchases or sales of financial assets are recognised and derecognised on a trade date basis. Regular way purchases or sales are purchases or sales of financial assets that require delivery of assets within the time frame established by regulation or convention in the marketplace.

Effective interest method

The effective interest method is a method of calculating the amortised cost of a debt instrument and of allocating interest income over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash receipts (including all fees on points paid or received that form an integral part of the effective interest rate, transaction costs and other premiums or discounts) through the expected life of the debt instrument, or, where appropriate, a shorter period to the net carrying amount on initial recognition.

Income is recognised on an effective interest basis for debt instruments other than financial assets classified as at fair value through profit or loss, of which interest income is included in net gains and losses.

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Loans and receivables (including trade and bills receivables, other receivables, pledged bank deposits, cash and bank balances) are measured at amortised cost using the effective interest method, less any impairment.

Impairment of financial assets

Financial assets, other than those at fair value through profit or loss, are assessed for indicators of impairment at the end of the reporting period. Financial assets are impaired where there is objective evidence that, as a result of one or more events that occurred after the initial recognition of the financial asset, the estimated future cash flows of the investment have been affected.

For certain categories of financial asset, such as trade receivables, assets that are assessed not to be impaired individually are assessed for impairment on a collective basis. Objective evidence of impairment for a portfolio of receivables could include the Group's past experience of collecting payments, an increase in the number of delayed payments in the portfolio past the average credit period of 180 days, as well as observable changes in national or local economic conditions that correlate with default on receivables.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2009

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Financial instruments (Continued)

Financial assets (Continued)

Impairment of financial assets (Continued)

For financial assets carried at amortised cost, the amount of the impairment is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the financial asset's original effective interest rate.

The carrying amount of the financial asset is reduced by the impairment loss directly for all financial assets with the exception of trade receivables, where the carrying amount is reduced through the use of an allowance account. When a trade receivable is considered uncollectible, it is written off against the allowance account. Subsequent recoveries of amounts previously written off are credited against the allowance account. Changes in the carrying amount of the allowance account are recognised in profit or loss.

For financial assets measured at amortised cost, if, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is reversed through profit or loss to the extent that the carrying amount of the investment at the date the impairment is reversed does not exceed what the amortised cost would have been had the impairment not been recognised.

Financial liabilities and equity

Debt and equity instruments issued by a group entity are classified as either financial liabilities or as equity in accordance with the substance of the contractual arrangements 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 an entity after deducting all of its liabilities. The Group's financial liabilities are generally classified into financial liabilities at fair value through profit or loss and other financial liabilities.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2009

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Financial instruments (Continued)

Financial liabilities and equity (Continued)

Effective interest method

The effective interest method is a method of calculating the amortised cost of a debt instrument and of allocating interest income over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments (including all fees on points paid or received that form an integral part of the effective interest rate, transaction costs and other premiums or discounts) through the expected life of the financial liability, or, where appropriate, a shorter period to the net carrying amount on initial recognition.

Interest expense is recognised on an effective interest basis other than financial liabilities classified as at fair value through profit or loss, of which interest expense is included in net gains and losses.

Financial liabilities at fair value through profit or loss

Financial liabilities are classified as at fair value through profit or loss when the financial liability is either held for trading or it is designated as at fair value through profit or loss on initial recognition.

A financial liability is classified as held for trading if:

- it has been acquired principally for the purpose of repurchasing it in the near term; or
- on initial recognition it is part of a portfolio of identified financial instruments that the Group manages together and has a recent actual pattern of short-term profit-taking; or
- it is a derivative that is not designated and effective as a hedging instrument.

A financial liability other than a financial liability held for trading may be designated as at fair value through profit or loss upon initial recognition if:

- such designation eliminates or significantly reduces a measurement or recognition inconsistency that would otherwise arise; or
- the financial liability forms part of a group of financial assets or financial liabilities or both, which is managed and its performance is evaluated on a fair value basis, in accordance with the Group's documented risk management or investment strategy, and information about the grouping is provided internally on that basis; or
- it forms part of a contract containing one or more embedded derivatives, and HKAS 39 permits the entire combined contract (asset or liability) to be designated as at fair value through profit or loss.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2009

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Financial instruments (Continued)

Financial liabilities and equity (Continued)

Financial liabilities at fair value through profit or loss (Continued)

Financial liabilities at fair value through profit or loss are stated at fair value, with any gains or losses arising on remeasurement recognised in profit or loss. The net gain or loss recognised in profit or loss includes any interest paid on the financial liabilities.

Other financial liabilities

Other financial liabilities (including trade and bills payables and other payables and accruals) 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.

Repurchase of the Company's own equity instruments is recognised and deducted directly in equity. No gain or loss is recognised in profit or loss on the purchase, sale, issue or cancellation of the Company's own equity instruments.

Derecognition

The Group derecognises a financial asset only when the contractual rights to the cash flows from the asset expire, or when a financial asset is transferred, the Group has transferred substantially all the risks and rewards of ownership of the asset to another entity. If the Group neither transfers nor retains substantially all the risks and rewards of ownership and continues to control the transferred asset, the Group recognises its retained interest in the asset and an associated liability for amounts it may have to pay. If the Group retains substantially all the risks and rewards of ownership of a transferred financial asset, the Group continues to recognise the financial asset and also recognises a collateralised borrowing for the proceeds received.

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 in other comprehensive income and accumulated in equity is recognised in profit or loss.

The Group derecognises financial liabilities when, and only when, the Group's obligations are discharged, cancelled or they expire. The difference between the carrying amount of the financial liability derecognised and the consideration paid and payable is recognised in profit or loss.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2009

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Research and development costs

Research costs are expensed as incurred. Development costs incurred on development projects relating to the design and testing of new or improved products are recognised as an intangible asset when it is probable that the project will be a success consisting its commercial and technological feasibility, and costs can be measured reliably. Such development costs are recognised as an asset and amortised from the commencement of the commercial production of the product on a straight-line basis over a period of not more than five years to reflect the pattern in which the related economic benefits are recognised. Development costs that do not meet the above criteria are expensed as incurred. Development costs previously recognised as an expense are not recognised as an asset in a subsequent period.

Inventories

Inventories are stated at the lower of cost and net realisable value. Cost is determined using the weighted average method. The cost of finished goods and work-in-progress comprises materials, direct labour and an appropriate proportion of all production overhead expenditure. Net realisable value is the estimated selling price in the ordinary course of business, less the estimated costs of completion and the estimated costs necessary to make the sale.

Cash and cash equivalents

Cash and cash equivalents includes cash in hand, deposits held at call with banks, other short-term highly liquid investments with original maturities of three months or less, and bank overdrafts.

Provisions

Provisions are recognised when the Group has a present obligation (legal or constructive) as a result of a past event, it is probable that the Group will be required to settle the obligation, and a reliable estimate can be made of the amount of the obligation.

The amount recognised as a provision is the best estimate of the consideration required to settle the present obligation at the end of the reporting period, taking into account the risks and uncertainties surrounding the obligation. Where a provision is measured using the cash flows estimated to settle the present obligation, its carrying amount is the present value of those cash flows (where the effect is material).

Contingent liabilities acquired in a business combination are initially measured at fair value at the date of acquisition. At the end of the reporting period, such contingent liabilities are measured at the higher of the amount that would be recognised in accordance with HKAS 37 and the amount initially recognised less cumulative amortization recognised in accordance with HKAS 18.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2009

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Income tax

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

The tax currently payable is based on taxable profit for the year. Taxable profit differs from profit as reported in the consolidated statement of comprehensive income because of items of income or expense that are taxable or deductible in other years and items that are never taxable or deductible. The Group's liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the end of the reporting period.

Deferred tax is recognised on temporary 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. Deferred tax liabilities are generally recognised for all taxable temporary differences. Deferred tax assets are generally recognised for all deductible temporary differences to the extent that it is probable that taxable profits will be available against which those deductible temporary differences can be utilised. Such deferred tax 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.

Deferred tax liabilities are recognised for taxable temporary differences associated with investments in subsidiaries and associates, except where the Group is able to control the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future. Deferred tax assets arising from deductible temporary differences associated with such investments and interests are only recognised to the extent that it is probable that there will be sufficient taxable profits against which to utilise the benefits of the temporary differences and they are expected to reverse in the foreseeable future.

The carrying amount of deferred tax assets is reviewed at the end of the reporting period 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 assets and liabilities are measured at the tax rates that are expected to apply in the period in which the liability is settled or the asset realised, based on tax rates (and tax laws) that have been enacted or substantively enacted by the end of the reporting period. The measurement of deferred tax liabilities and assets reflects the tax consequences that would follow from the manner in which the Group expects, at the end of the reporting period, to recover or settle the carrying amount of its assets and liabilities. Deferred tax is recognised in profit or loss, except when it relates to items that are recognised in other comprehensive income or directly in equity, in which case, the deferred tax is also recognised in other comprehensive income or directly in equity respectively.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2009

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Revenue recognition

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

Revenue from the sale of goods is recognised when all the following conditions are satisfied:

- the Group has transferred to the buyer the significant risks and rewards of ownership of the goods;
- the Group retains neither continuing managerial involvement to the degree usually associated with ownership nor effective control over the goods sold;
- the amount of revenue can be measured reliably;
- it is probable that the economic benefits associated with the transaction will flow to the Group; and
- the costs incurred or to be incurred in respect of the transaction can be measured reliably.

Interest income from a financial asset (other than a financial asset at fair value through profit or loss) 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 estimated future cash receipts through the expected life of the financial asset to that asset's net carrying amount on initial recognition.

Employee benefits

Employee leave entitlements

Employee entitlements to annual leave are recognised when they accrue to employees. A provision is made for the estimated liability for annual leave as a result of services rendered by employees up to the balance sheet date. Employee entitlements to sick leave and maternity leave are not recognised until the time of leave.

Pension obligations

Payments to defined contribution retirement plans are charged as an expense when employees have rendered service entitling them to the contributions.

Borrowings

Borrowings are recognised initially at fair value, net of transaction costs incurred. Borrowings are subsequently stated at amortised cost; any difference between the proceeds (net of transaction costs) and the redemption value is recognised in profit or loss over the period of the borrowings using the effective interest method.

Borrowings are classified as current liabilities unless the Group has an unconditional right to defer settlement of the liability for at least 12 months after the end of the reporting period.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2009

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Government grants

Grants from the government are recognised at their fair value where there is a reasonable assurance that the grants will be received.

Government grant relating to purchase of property, plant and equipment is included in non-current liabilities as deferred income and is expensed in profit or loss on a straight-line basis over the expected useful lives of the related assets.

Foreign and presentation currency

Functional and presentation currency

Items included in the accounts of the Group are measured using the currency of the primary economic environment in which the entity operates ("the functional currency"). The accounts are presented in RMB, which is the Group's functional and presentation currency.

Transactions and balances

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the consolidated statement of comprehensive income.

Dividend distribution

Dividend distribution to the Company's shareholders is recognised as a liability in the Group's accounts in the period in which the dividends are approved by the Company's shareholders.

Related party transactions

A party is considered to be related to the Group if:

(a) the party, directly or indirectly through one or more intermediaries, (i) controls, is controlled by, or is under common control with, the Group; (ii) has an interest in the Group that gives it significant influence over the Group; or (iii) has joint control over the Group;

(b) the party is an associate;

(c) the party is a jointly-controlled entity;

(d) the party is a member of the key management personnel of the Group or its parent;

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2009

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Related party transactions (Continued)

(e) the party is a close member of the family of any individual referred to in (a) or (d);

(f) the party is an entity that is controlled, jointly controlled or significantly influenced by or for which significant voting power in such entity resides with, directly or indirectly, any individual referred to in (d) or (e); or

(g) the party is a post-employment benefit plan for the benefit of the employees of the Group, or of any entity that is a related party of the Group.

A transaction is considered to be a related party transaction when there is a transfer of resources or obligations between related parties.

4. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS

Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

The Group makes estimates and judgements concerning the future. The resulting accounting estimates will, by definition, seldom equal the related actual results. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below.

Estimated impairment of purchased technical know-how

The Group assesses annually whether purchased technical know-how has suffered any impairment, in accordance with the accounting policy stated in Note 3. The recoverable amounts have been determined based on value-in-use calculations. These calculations require estimation on future cash flow generated from these purchased technical know-how.

Taxation

The Group is subject to PRC enterprise income tax and value-added tax. Since PRC tax rules are complicated and there may be new PRC tax rules and regulations from time to time, the Group recognised tax liabilities based on estimates of tax liabilities. Where the final tax outcome is different from the amounts that were initially recorded, such differences will impact the income tax and deferred tax provisions in the period in which such determination is made.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2009

4. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS (Continued)

Useful lives of property, plant and equipment

In accordance with HKAS 16, the Group estimates the useful lives of property, plant and equipment in order to determine the amount of depreciation expenses to be recorded. The useful lives are estimated at the time the asset is acquired based on historical experience, the expected usage, wear and tear of the assets, as well as technical obsolescence arising from changes in the market demands. The Group also performs annual reviews on whether the assumptions made on useful lives continue to be valid.

Provision for obsolete inventories

The management of the Group reviews an aging analysis at the end of each reporting period, and makes provision for obsolete and slow-moving inventory items. The management estimates the net realisable value for such finished goods based primarily on the latest invoice prices and current market conditions. The Group carries out an inventory review on a product-by-product basis at the end of each reporting period and makes provision for obsolete items.

Trade and other receivables

The debt profile of trade and other debtors is reviewed on a regular basis to ensure that the trade and other debtor balances are collectible and follow up actions are promptly carried out if the agreed credit periods have been exceeded. However from time to time, the Group may experience delays in collection. Where recoverability of trade and other debtor balances are called into doubts, specific provisions for trade and other receivables are made based on credit status of the debtors, the aged analysis of the receivable balances and write-off history. Certain receivables may be initially identified as collectible, yet subsequently become uncollectible and result in a subsequent write-off of the related receivable to the consolidated statement of comprehensive income. Changes in the collectibility of trade and other receivables for which provision are not made could affect the results of operations.

Fair value of financial instruments

The fair value of financial instruments that are not traded in an active market is determined by valuation techniques. The Group uses its judgement to select a variety of methods and make assumptions that are primarily based on market conditions existing at the end of each reporting period.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2009

5. FINANCIAL INSTRUMENTS AND CAPITAL RISK MANAGEMENT

(a) *Categories of financial instruments*

	As at 31 December	
	2009	2008
	RMB'000	RMB'000
Financial assets		
Loan and receivables (including cash and cash equivalents)	**570,124**	217,572
Financial liabilities		
Amortised cost	**416,352**	127,838

(b) *Financial risk management objectives and policies*

The main risks arising from the Group's financial instruments are market risk (including interest rate risk and foreign currency risk), credit risk and liquidity risk. The Board of Directors review and agree policies for managing each of these risks and they are summarised below.

There has been no change to the types of the Group's exposure in respect of financial instruments or the manner in which it manages and measures the risks.

Market risk

The Group's activities expose it primarily to the financial risks of changes in interest rates and foreign currency exchange rates.

Interest rate risk management

The Group considers that there is no significant cash flow interest rate risk and fair value interest rate risk as the Group does not have variable rate and fixed rate borrowings. The Group did not enter into interest rate swap to hedge against its exposures to changes in fair values of the borrowings.

The Group's exposure to market risk for changes in interest rates relates primarily to the cash and bank balances. Floating-rate interest income is charged to the consolidated statement of comprehensive income as incurred.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2009

5. FINANCIAL INSTRUMENTS AND CAPITAL RISK MANAGEMENT

(Continued)

(b) ***Financial risk management objectives and policies*** (Continued)

Market risk (Continued)

Foreign currency risk management

The Group operates and conducts business in the PRC and all the Group's transactions, assets and liabilities are primarily denominated in RMB and Hong Kong dollars ("HKD"), which expose the Group to foreign currency risk. The Group does not have any formal hedging policy.

The carrying amounts of the Group's foreign currency denominated monetary assets at the end of the reporting period are as follows:

	As at 31 December	
	2009	2008
	RMB'000	RMB'000
Assets		
HKD	**739**	39

Sensitivity analysis on foreign currency

The following table details the Group's sensitivity to a 5% increase and decrease in RMB against the relevant foreign currency. 5% is the sensitivity rate used when reporting foreign currency risk internally to key management personnel and represents management's assessment of the reasonably possible change in foreign exchange rates. The sensitivity analysis includes outstanding foreign currency denominated monetary items and adjusts their translation at the year end for a 5% change in foreign currency rates. A negative number below indicates a decrease in profit where RMB strengthen 5% against the relevant currency. For a 5% weakening of RMB against the relevant currency, there would be an equal and opposite impact on the profit, and the balance below would be positive.

	As at 31 December	
	2009	2008
	RMB'000	RMB'000
Impact of HKD		
Profit or loss #	**(37)**	(2)

This is mainly attributable to the exposure outstanding on cash and bank balances denominated in HKD not subject to cash flow hedge at the end of the reporting period.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2009

5. FINANCIAL INSTRUMENTS AND CAPITAL RISK MANAGEMENT

(Continued)

(b) ***Financial risk management objectives and policies*** (Continued)

Credit risk

As at 31 December 2009, the Group's maximum exposure to credit risk which will cause a financial loss to the Group due to failure to discharge an obligation by the counterparties is arising from the carrying amount of the respective recognised financial assets as stated in the consolidated statement of financial position.

The Group has put in place policies to ensure that sales of products are made to customers with an appropriate credit history and the Group performs periodic credit evaluation of its customers. The Group's historical experience in collection of trade and other receivables falls within the recorded allowances and the Directors are of the opinion that adequate provision for uncollectible trade and other receivables has been made in the accounts. In this regard, the Directors of the Company consider that the Group's credit risk is significantly reduced.

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

Other than concentration of credit risk on liquid funds which are deposited with several banks with high credit ratings, the Group does not have any other significant concentration of credit risk. Trade receivables consist of a large number of customers.

Liquidity risk

Ultimate responsibility for liquidity risk management rests with the Board of Directors, which has built an appropriate liquidity risk management framework to meet the Group's short, medium and long-term funding and liquidity management requirements. The Group manages liquidity risk by maintaining adequate reserves, by continuously monitoring forecast and actual cash flows and matching the maturity profiles of financial assets and liabilities.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2009

5. FINANCIAL INSTRUMENTS AND CAPITAL RISK MANAGEMENT

(Continued)

(b) *Financial risk management objectives and policies* (Continued)

Liquidity risk (Continued)

The following table details the Group's remaining contractual maturity for its financial liabilities based on the agreed repayment terms. The tables have been drawn up based on the undiscounted cash flows of financial liabilities based on the earliest date on which the Group can be required to pay. The tables include both interest and principal cash flows.

	Weighted average effective interest rate %	Within 1 year RMB'000	Over 1 year RMB'000	Total undis-counted cash flows RMB'000	Total carrying amount RMB'000
As at 31 December 2009					
Non-derivative financial liabilities					
Trade and bills payables	–	**328,995**	–	**328,995**	**328,995**
Other payables and accruals	–	**74,867**	–	**74,867**	**74,867**
Dividend payable	–	**7,314**	–	**7,314**	**7,314**
Deposits received	–	**5,176**	–	**5,176**	**5,176**
		416,352	–	**416,352**	**416,352**
As at 31 December 2008					
Non-derivative financial liabilities					
Trade and bills payables	–	65,854	–	65,854	65,854
Other payables and accruals	–	57,160	–	57,160	57,160
Deposits received	–	4,824	–	4,824	4,824
		127,838	–	127,838	127,838

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2009

5. FINANCIAL INSTRUMENTS AND CAPITAL RISK MANAGEMENT

(Continued)

(b) Financial risk management objectives and policies (Continued)

Fair value of financial instruments

The fair value of financial assets and financial liabilities are determined as follows:

(i) the fair value of financial assets and financial liabilities with standard terms and conditions and traded in active markets are determined with reference to quoted market bid prices and ask prices respectively.

(ii) the fair value of other financial assets and financial liabilities (excluding derivative instruments) are determined in accordance with generally accepted pricing models (e.g. discounted cash flow analysis using observable and/or unobservable inputs).

(iii) The fair values of derivative instruments are calculated using quoted prices. Where such prices are not available, a discounted cash flow analysis is performed using the applicable yield curve for the duration of the instruments for non-optional derivatives, and option pricing models for optional derivatives.

The Group's financial instruments that are measured subsequent to initial recognition at fair value are grouped into Levels 1 to 3 based on the degree to which the fair value is observable:

- Level 1 fair value measurements are those derived from quoted prices (unadjusted) in active markets for identical assets or liabilities;

- Level 2 fair value measurements are those derived from inputs other than quote prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices); and

- Level 3 fair value measurements are those derived from valuation techniques that include inputs for the asset or liability that are not based on observable market data (unobservable inputs).

No analysis is disclosed since the Group has no financial instruments that are measured subsequent to initial recognition at fair value at the end of the reporting period.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2009

5. FINANCIAL INSTRUMENTS AND CAPITAL RISK MANAGEMENT

(Continued)

(c) Capital risk management

The Group's objectives when managing capital are to provide returns for shareholders and benefits for other stakeholders and to maintain an optimal capital structure to reduce the cost of capital.

The capital structure of the Group consists of debt (which includes bank borrowings), and equity attributable to owners of the Company, comprising issued share capital, reserves and retained earnings.

Gearing ratio

The Directors of the Company review the capital structure regularly. As part of this review, the Directors consider the cost of capital and the risk associated with each class of capital. During the year ended 31 December 2009, the Group's strategy, which was unchanged from previous years, was to reduce the gearing ratio. This ratio is calculated base on total debt and total assets.

The gearing ratio as at 31 December 2009 and 2008 are as follows:

	As at 31 December	
	2009	2008
	RMB'000	RMB'000
Total debt	**–**	–
Total assets	**1,220,473**	681,722
Gearing ratio	**N/A**	N/A

6. SEGMENT INFORMATION

The Group has adopted HKFRS 8 *Operating Segments* with effect from 1 January 2009. HKFRS 8 is a disclosure standard that requires operating segments to be identified on the basis of internal reports about components of the Group that are regularly reviewed by the chief operating decision makers for the purposes of allocating resources to segments and assessing their performance. In contrast, the predecessor standard (HKAS 14 *Segment Reporting*) required an entity to identify two sets of segments (business and geographical) using a risks and returns approach. In the past, the Group's primary reporting segment was business segments.

In prior years, the principal activities of the Group are manufacturing and sales of pharmaceutical products. No business or geographical segment analysis is presented as all operations, assets and liabilities of the Group were related to manufacturing and sales of pharmaceutical products, and all assets and customers were located in the PRC.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2009

6. SEGMENT INFORMATION (Continued)

The Group currently operates in one business segment in the manufacturing and sales of pharmaceutical products in the PRC. A single management team reports to the chief operating decision makers who comprehensively manage the entire business. The reportable operating results report to the chief operating decision makers are the net profit of the Group and the reportable assets and liabilities report to the chief operating decision makers are the Group's assets and liabilities. Accordingly, the Group does not have separately reportable segments in accordance with HKFRS 8.

Information about major customers

Included in revenues arising from sales of pharmaceutical products of approximately RMB907,453,000 (2008: RMB667,792,000) are revenues of approximately RMB119,688,000 (2008: RMB56,890,000) which arose from sales to the Group's largest customer.

7. TURNOVER AND OTHER REVENUE

Turnover and other revenue recognised are as follows:

	2009 RMB'000	2008 RMB'000
Turnover		
Sales of manufactured pharmaceutical products	907,453	667,792
Other revenue		
Interest income on bank deposits	2,191	842
Sundry income	1,576	1,771
	3,767	2,613
Total revenue	911,220	670,405

8. FINANCE COSTS

	2009 RMB'000	2008 RMB'000
Bills payables wholly repayable within six months	240	–
Bank loans wholly repayable within five years	–	1,250
	240	1,250

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2009

9. PROFIT FROM OPERATIONS

	2009 RMB'000	2008 RMB'000
Operating profit of the Group was determined after charging/(crediting) the following:		
Raw materials and consumables used	**476,278**	346,892
Changes in inventories of finished goods and work-in-progress	**(50,270)**	(30,837)
Depreciation of property, plant and equipment (Note 20)	**17,203**	13,030
Loss on disposal of property, plant and equipment	**–**	283
Amortisation of prepaid lease payments (Note 22)	**274**	273
Amortisation of purchased technical know-how (included in cost of sales) (Note 18)	**844**	935
Write-off of obsolete inventories (Note 25)	**1,377**	879
Impairment loss recognised in respect of prepayments to acquire technical know-how (Note 19)	**2,430**	170
Impairment loss recognised in respect of trade receivables (Note 26)	**1,861**	535
Impairment loss recognised in respect of other receivables (Note 27)	**541**	433
Employees benefit expenses (excluding Directors' and supervisors' remuneration)	**85,301**	55,228
Research and development costs	**14,902**	3,527
Advertising costs	**2,678**	2,637
Auditors' remuneration	**480**	480
and other crediting:		
Other income		
Government subsidy	**–**	177
Penalty income	**973**	2,103
Reversal of obsolete inventories written down (Note 25)	**878**	354
Reversal of impairment loss recognised in respect of trade receivables (Note 26)	**266**	215
Reversal of impairment loss recognised in respect of other receivables (Note 27)	**217**	45
Gain on disposal of property, plant and equipment	**167**	–
	2,501	2,894

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2009

10. TAXATION

(i) No provision for Hong Kong profits tax has been made as the Group did not carry on any business in Hong Kong during the year (2008: Nil).

(ii) As described in the paragraph below, the Group is subject to the PRC enterprise income tax at a rate of 15% for year 2009 (2008: 25%).

On 12 November 2009, the Company received confirmation from the Recognition Authority that the Company has been recognised as the High and New Technology Enterprise on 12 June 2009. Pursuant to the new Enterprise Income Tax Law, the enterprise income tax applicable to the High and New Technology Enterprise is reduced to be levied at 15%. The Company has since been enjoying the tax concession rate of 15% for three years effective from 1 January 2009.

(iii) The PRC value-added tax

The Group is subject to the PRC value-added tax ("VAT") at 17% (2008: 17%) of revenue from sale of goods in the PRC. Input VAT paid on purchases can be used to offset output VAT levied on sales to determine the net VAT recoverable/payable.

(iv) The amount of taxation charged to the consolidated statement of comprehensive income represents:

	2009	2008
	RMB'000	RMB'000
Current taxation – Enterprise income tax	**47,137**	61,495
Deferred taxation (Note 23)	**(421)**	1,003
	46,716	62,498

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2009

10. TAXATION (Continued)

The taxation on the Group's profit before taxation differs from the theoretical amount that would arise using the taxation rate in the PRC as follows:

	2009 RMB'000	2008 RMB'000
Profit before taxation	315,266	245,653
Calculated at a taxation rate of 25% (2008: 25%)	78,817	61,411
Tax effect of income not taxable for tax purpose	(388)	(389)
Tax effect of expenses not deductible for tax purpose	830	925
Tax effect of tax concession	(31,527)	–
Tax effect of share of profit of associate	(1,016)	(99)
Decrease in opening deferred tax asset resulting from a decrease in applicable tax rate	–	650
Taxation charge for the year	46,716	62,498

11. DIVIDENDS

A dividend in respect of 2009 of RMB0.02 per share, amounting to a total dividend of RMB12,192,000 (2008: RMB12,192,000) is to be proposed at the annual general meeting of the Company on 8 June 2010. The consolidated financial statements do not reflect this dividend payable.

	2009 RMB'000	2008 RMB'000
Proposed final dividend of RMB0.02 (2008: RMB0.02) per ordinary share	12,192	12,192

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2009

12. EMPLOYEE BENEFIT EXPENSES

	2009	2008
	RMB'000	RMB'000
Salaries and wages	**42,742**	32,873
Sales commission	**37,122**	16,625
Pension costs – defined contribution plans	**5,437**	5,730
	85,301	55,228

13. PENSION AND RETIREMENT BENEFIT COSTS

The Group has provided for pension and retirement benefit costs to all qualified employees in the PRC in accordance with the regulations set by the PRC local government which is calculated based on 30% on the employees' salary or the monthly average salaries set out by the PRC local government.

Commencing 2003, the Group has participated in a Mandatory Provident Fund Scheme (the "MPF Scheme") in Hong Kong for all qualified Hong Kong employees, which is a defined contribution scheme managed by independent trustees. Monthly contributions are made to the MPF Scheme based on 5% of the Hong Kong employees' relevant income as defined under the Mandatory Provident Fund Schemes Ordinance. Both the Group's and the employees' contributions are subject to a cap of RMB882 (equivalent to HK$1,000) per month and thereafter contributions are voluntary.

During the year ended 31 December 2009, the Group has contributed approximately RMB10,580 (2008: RMB10,555) to the MPF Scheme.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2009

14. DIRECTORS', SUPERVISORS' AND SENIOR MANAGEMENT'S EMOLUMENTS

(i) The aggregate amounts of emoluments paid and payable to the Directors and supervisors of the Company are as follows:

	2009 RMB'000	2008 RMB'000
Basic salaries and allowances	991	963
Retirement benefit costs	166	165
	1,157	1,128

Individual emoluments paid and payable to the Directors and supervisors for the year are as follows:

	2009 RMB'000	2008 RMB'000
Executive Directors		
Liu Baoqi	456	456
Li Minghua	127	127
Liu Zhenhai	106	106
Han Fengsheng	67	67
Chen Yu (appointed on 28 April 2009)	45	–
Non-executive Directors		
Zhou Wuxian (resigned on 28 April 2009)	8	24
Yin Chuangui	24	24
Liu Yuxin	24	24
Independent non-executive Directors		
Foo Tin Chung, Victor	120	120
Fu Hongzheng	24	24
Li Hongjian	24	24
Supervisors		
Sun Song	60	60
Zhu Enqiang	24	24
Gao Xiaoling	24	24
Guan Yonghua	24	24
	1,157	1,128

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2009

14. DIRECTORS', SUPERVISORS' AND SENIOR MANAGEMENT'S EMOLUMENTS (Continued)

(i) The aggregate amounts of emoluments paid and payable to the Directors and supervisors of the Company are as follows: (continued)

The number of Directors and supervisors whose emoluments fell within the following band is as follows:

	Number of individuals	
	2009	2008
Nil – RMB881,679 (equivalent to Nil – HK$1,000,000)	**15**	14

None of the Directors have waived any emoluments during the year.

(ii) The five individuals whose emoluments were the highest in the Group for the year include four (2008: four) Directors whose emoluments are reflected in the analysis presented above. The emoluments payable (excluding amounts paid or payable by way of commissions on sales generated by the individual) to the remaining one (2008: one) non-director, highest paid individual during the year are as follows:

	2009	2008
	RMB'000	RMB'000
Basic salaries and allowances	**660**	660
Retirement benefit costs	**12**	12
	672	672

The number of non-director, highest paid individuals whose emoluments fell within the following band is as follows:

	Number of individuals	
	2009	2008
Nil – RMB881,679 (equivalent to Nil – HK$1,000,000)	**1**	1

(iii) During the year, no emoluments have been paid to the Directors of the Company or the five highest individuals as an inducement to join or as compensation for loss of office (2008: Nil).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2009

15. EARNINGS PER SHARE

Basic earnings per share is calculated by dividing the profit attributable to owners of the Company by the weighted average number of ordinary shares in issue during the year.

	2009	2008
Profit attributable to owners of the Company (RMB'000)	268,550	183,155
Weighted average number of ordinary shares in issue ('000)	609,600	609,600
Basic and diluted earnings per share (RMB)	0.441	0.300

16. INTEREST IN A SUBSIDIARY

The Company

	2009 RMB'000	2008 RMB'000
Cost of investment in a subsidiary, unlisted in PRC	459	–

As at 31 December 2009, the Company had interest in the following subsidiary:

Name of the entity	Form of business structure	Place of incorporation and operation	Proportion of registered capital held by the Company	Proportion of voting power held	Principal activities
Sichuan Luoxin Pharmacy Company Limited* (四川羅欣醫藥有限公司) ("Sichuan Luoxin")	Incorporated	PRC	51%	51%	Wholesale and manufacture of biochemical products and Chinese medicine

The subsidiary had no debt securities outstanding at the end of the reporting period or at any time during the year.

* The English name represents the translated name of the subsidiary as no English name has been registered.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2009

17. INTEREST IN AN ASSOCIATE

The Group and the Company

	2009 RMB'000	2008 RMB'000
Cost of investment in an associate, unlisted in the PRC	**19,620**	19,620
Share of post-acquisition profits and other comprehensive income, net of dividends received *(Note)*	**7,170**	3,107
	26,790	22,727

As at 31 December 2009 and 2008, the Group and the Company had interest in the following associate:

Name of the entity	Form of business structure	Place of incorporation and principal operation	Proportion of registered capital held by the Group	Proportion of voting power held	Principal activities
Qilu Medical Investment Management Limited	Incorporated	PRC	20%	20%	Management and consultation of medical related business

The summarised financial information in respect of the associate is set out below:

	2009 RMB'000	2008 RMB'000
Total assets	**179,229**	190,623
Total liabilities	**(45,279)**	(76,992)
Net assets	**133,950**	113,631
Share of net assets of associate	**26,790**	22,727
Revenue	**16,290**	5,203
Profit for the year	**20,318**	1,974
Share of profit of associate for the year	**4,063**	395

Note:

The amount includes (i) the accumulated share of profit of associate of approximately RMB4,458,000 (2008: RMB395,000) for the year ended 31 December 2009; and (ii) excess of the share of the net fair value of the associate's identifiable assets, liabilities and contingent liabilities over the cost of the investment in associate of approximately RMB2,712,000. The Group has reassessed the fair value of the associate's identifiable net assets and considered the value of net assets are measured reliably.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2009

18. PURCHASED TECHNICAL KNOW-HOW

The Group and the Company

	RMB'000
Cost:	
At 1 January 2008	15,300
Additions	2,000
At 31 December 2008 and 1 January 2009	17,300
Additions	150
At 31 December 2009	17,450
Accumulated amortisation and impairment:	
At 1 January 2008	13,675
Charge for the year	935
At 31 December 2008 and 1 January 2009	14,610
Charge for the year	844
At 31 December 2009	15,454
Net book value:	
At 31 December 2009	1,996
At 31 December 2008	2,690

19. PREPAYMENTS TO ACQUIRE TECHNICAL KNOW-HOW

The Group and the Company

As at 31 December 2009 and 2008, the amounts are prepayments to third parties to acquire technical know-how. During the year ended 31 December 2009, amount of RMB2,430,000 (2008: RMB170,000) was impaired. The Directors of the Company have considered that the amount of the prepayment to acquire technical know-how was not recoverable as the research and development process was not successful and would not bring any future economic benefit to the Group and the Company.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2009

20. PROPERTY, PLANT AND EQUIPMENT

The Group

	Buildings	Plant and machinery	Motor vehicles	Office equipment	Total
	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000
Cost:					
At 1 January 2008	63,760	66,071	7,881	6,618	144,330
Additions	3,622	4,459	1,657	1,215	10,953
Disposals	(499)	(2,159)	(732)	(3)	(3,393)
Transfer from construction–in-progress (Note 21)	96,308	45,687	–	–	141,995
At 31 December 2008 and 1 January 2009	163,191	114,058	8,806	7,830	293,885
Additions	4,156	4,505	2,312	2,045	13,018
Transfer from construction–in-progress (Note 21)	8,607	10,071	–	–	18,678
Acquisition through business combination	–	–	–	5	5
Disposals	(4,083)	(2,286)	(1,539)	(27)	(7,935)
At 31 December 2009	171,871	126,348	9,579	9,853	317,651
Accumulated depreciation and impairment:					
At 1 January 2008	3,709	19,502	3,680	4,257	31,148
Charge for the year	2,553	8,309	1,365	803	13,030
Written back on disposals	(71)	(716)	(402)	(2)	(1,191)
At 31 December 2008 and 1 January 2009	6,191	27,095	4,643	5,058	42,987
Charge for the year	3,988	10,945	1,386	884	17,203
Written back on disposals	(185)	(1,375)	(1,176)	(24)	(2,760)
At 31 December 2009	9,994	36,665	4,853	5,918	57,430
Net book value:					
At 31 December 2009	**161,877**	**89,683**	**4,726**	**3,935**	**260,221**
At 31 December 2008	157,000	86,963	4,163	2,772	250,898

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2009

20. PROPERTY, PLANT AND EQUIPMENT (Continued)

As at 31 December 2009 and 2008, all buildings of the Group are located in the PRC.

Depreciation expense of RMB12,306,000 (2008: RMB10,079,000) have been expensed in cost of sales and RMB4,897,000 (2008: RMB2,951,000) have been included in administrative expenses for the year.

The Company

	Buildings	**Plant and machinery**	**Motor vehicles**	**Office equipment**	**Total**
	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000
Cost:					
At 1 January 2008	63,760	66,071	7,881	6,618	144,330
Additions	3,622	4,459	1,657	1,215	10,953
Disposals	(499)	(2,159)	(732)	(3)	(3,393)
Transfer from construction-in-progress (Note 21)	96,308	45,687	–	–	141,995
At 31 December 2008 and 1 January 2009	163,191	114,058	8,806	7,830	293,885
Additions	4,156	4,505	2,312	2,045	13,018
Transfer from construction-in-progress (Note 21)	8,607	10,071	–	–	18,678
Disposals	(4,083)	(2,286)	(1,539)	(27)	(7,935)
At 31 December 2009	171,871	126,348	9,579	9,848	317,646
Accumulated depreciation and impairment:					
At 1 January 2008	3,709	19,502	3,680	4,257	31,148
Charge for the year	2,553	8,309	1,365	803	13,030
Written back on disposals	(71)	(716)	(402)	(2)	(1,191)
At 31 December 2008 and 1 January 2009	6,191	27,095	4,643	5,058	42,987
Charge for the year	3,988	10,945	1,386	884	17,203
Written back on disposals	(185)	(1,375)	(1,176)	(24)	(2,760)
At 31 December 2009	9,994	36,665	4,853	5,918	57,430
Net book value:					
At 31 December 2009	**161,877**	**89,683**	**4,726**	**3,930**	**260,216**
At 31 December 2008	157,000	86,963	4,163	2,772	250,898

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2009

21. CONSTRUCTION-IN-PROGRESS

The Group and the Company

	RMB'000
At 1 January 2008	82,429
Additions	59,566
Transfer to property, plant and equipment (Note 20)	(141,995)
At 31 December 2008 and 1 January 2009	–
Additions	27,971
Transfer to property, plant and equipment (Note 20)	(18,678)
At 31 December 2009	**9,293**

Analysis of construction-in-progress as follows:

	2009	2008
	RMB'000	RMB'000
Construction cost of buildings	**2,241**	–
Cost of plant and machinery	**7,052**	–
	9,293	–

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2009

22. PREPAID LEASE PAYMENTS

The Group and the Company

Prepaid lease payments represent 50-year land use rights in the PRC expiring from November 2050 to July 2053. This payment is recognised as an expense over the leasehold period.

	RMB'000
At 1 January 2008	11,721
Amortisation of prepaid lease payments	(273)
At 31 December 2008 and 1 January 2009	11,448
Amortisation of prepaid lease payments	(274)
At 31 December 2009	**11,174**

Analysed for reporting purposes as:

	2009 RMB'000	2008 RMB'000
Current assets (included in other receivables, deposits and prepayments)	273	273
Non-current assets	10,901	11,175
	11,174	11,448

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2009

23. DEFERRED TAX ASSETS

The Group and the Company

Deferred taxation is calculated in full on temporary differences under the liability method using a principal taxation rate of 25% (2008: 25%).

The movements in the deferred tax assets are as follows:

	2009	2008
	RMB'000	RMB'000
At the beginning of the year	**1,682**	2,685
Deferred taxation credited/(charged) to the consolidated statement of comprehensive income (Note 10)	**421**	(1,003)
At the end of the year	**2,103**	1,682

	Provisions	**Amortisation charge on purchased technical know-how**	**Others**	**Total**
	RMB'000	RMB'000	RMB'000	RMB'000
At 1 January 2008	900	1,379	406	2,685
Effect of change in tax rate	(218)	(334)	(98)	(650)
(Charged)/credited to the consolidated statement of comprehensive income	74	(119)	(308)	(353)
At 31 December 2008 and 1 January 2009	756	926	–	1,682
Credited/(charged) to the consolidated statement of comprehensive income	605	(184)	–	421
At 31 December 2009	**1,361**	**742**	**–**	**2,103**

All deferred tax assets are to be recovered after more than 12 months.

There is no unprovided deferred taxation during the year.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2009

24. GOODWILL

The Group

	2009 RMB'000	2008 RMB'000
The carrying amount of goodwill was allocated to cash-generating unit as follows:		
Manufacturing and sales of pharmaceutical products	165	–

At the end of the reporting period, the Group assessed the recoverable amount of goodwill, and determined that goodwill associated with the Group's manufacturing and sales of pharmaceutical products activity was not impaired. The recoverable amount was assessed by reference to the cash-generating unit's value in use.

The recoverable amount of this cash-generating unit is determined based on a value in use calculation which uses cash flow projections based on financial budgets approved by the Directors covering a five-year period, and a discount rate of 12%.

Cash flow projections during the budget period are based on the same expected gross margins and raw material price inflation throughout the budget period. The Directors believe that any reasonably possible change in the key assumptions on which the recoverable amount is based would not cause the carrying amount of the unit to exceed the aggregate recoverable amount of the cash-generating unit.

25. INVENTORIES

The Group and the Company

	2009 RMB'000	2008 RMB'000
Raw materials	117,183	51,628
Work-in-progress	61,138	40,500
Finished goods	69,722	40,090
	248,043	132,218
Less: Write-down of obsolete inventories	(1,439)	(940)
	246,604	131,278

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2009

25. INVENTORIES (Continued)

The cost of inventories recognised as expense and included in cost of sales amounted to approximately RMB426,008,000 (2008: RMB316,055,000).

Movements in the write down of obsolete inventories are as follows:

	2009 RMB'000	2008 RMB'000
Balance at the beginning of the year	**940**	415
Write-down of obsolete inventories during the year	**1,377**	879
Reversal of obsolete inventories written down	**(878)**	(354)
Balance at the end of the year	**1,439**	940

The reversal of obsolete inventories written down arose from sales of obsolete inventories recognised during the year.

The Directors of the Company have assessed the net realisable values and conditions of the Group's and the Company's inventories as at 31 December 2009 and have considered a write down of obsolete inventories of approximately RMB1,439,000 (2008: RMB940,000) be made in respect of the net realisable value of the inventories.

26. TRADE AND BILLS RECEIVABLES

The Group and the Company

	2009 RMB'000	2008 RMB'000
Trade receivables	**50,235**	58,249
Bills receivables	**18,632**	11,037
	68,867	69,286
Less: Provision for impairment loss recognised in respect of trade receivables	**(2,679)**	(1,084)
	66,188	68,202

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2009

26. TRADE AND BILLS RECEIVABLES (Continued)

The following is an analysis of trade and bills receivables by age, presented based on the invoice date, net of provision for impairment loss:

	2009	2008
	RMB'000	RMB'000
1 to 90 days	**32,343**	33,925
91 to 180 days	**28,359**	24,271
181 to 365 days	**5,486**	10,006
	66,188	68,202

Customers are generally granted with credit term of 180 days. Bills receivables are all due to mature within 180 days. Trade and bills receivables as at 31 December 2009 are denominated in RMB.

As at 31 December 2009, amount of approximately RMB6,977,000 and RMB673,000 is receivable from a shareholder and a related company respectively (Note 37). The amounts due are unsecured, interest-free and receivable within 180 days.

As at 31 December 2008, amount of approximately RMB7,034,000 is receivable from a related company (Note 37). The amount due is unsecured, interest-free and receivable within 180 days.

(a) Included in the Group's and the Company's trade and bills receivables balance are debtors with a carrying amount of approximately RMB5,486,000 (2008: RMB10,006,000) which are past due at the reporting date for which the Group has not provided for impairment loss. The Group and the Company have recognised provision for impairment loss of 100% against all receivables over 365 days because historical experience has been that receivables that are past due beyond 365 days are not recoverable. The Group and the Company does not hold any collateral over these balances.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2009

26. TRADE AND BILLS RECEIVABLES (Continued)

(a) (Continued)

Details of the aging analysis of trade and bills receivables which are past due but not impaired are as follows:

	2009 RMB'000	2008 RMB'000
181 to 365 days	**5,486**	10,006

(b) Movements in the provision for impairment loss recognised in respect of trade receivables are as follows:

	2009 RMB'000	2008 RMB'000
Balance at the beginning of the year	**1,084**	784
Bad debt written off	**–**	(20)
Impairment loss recognised during the year	**1,861**	535
Reversal of impairment loss recognised in respect of trade receivables	**(266)**	(215)
Balance at the end of the year	**2,679**	1,084

In determining the recoverability of trade receivables, the Group and the Company consider any change in the credit quality of the trade receivables from the date credit were initially granted up to the reporting date. Accordingly, the Directors of the Company have considered provision for impairment is values be made in respect of trade receivables to their recoverable values and believed that there is no further credit provision required in excess of the provision for impairment loss recognised in respect of trade receivables.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2009

27. OTHER RECEIVABLES, DEPOSITS AND PREPAYMENTS

The Group

	2009 RMB'000	2008 RMB'000
Other receivables and deposits	4,887	4,912
Prepayments (Note)	84,186	33,600
	89,073	38,512
Less: Provision for impairment loss recognised in respect of other receivables	(1,324)	(1,000)
	87,749	37,512

Note:

Prepayments mainly comprised of prepayment of value-added tax, acquisition of raw materials, packing materials and consumables, and acquisition of prepaid lease payments of approximately RMB16,012,000 (2008: RMB15,664,000), RMB52,367,000 (2008: RMB8,988,000) and RMB10,023,000 (2008: RMB5,000,000) respectively.

Movements in the provision for impairment loss recognised in respect of other receivables are as follows:

	2009 RMB'000	2008 RMB'000
Balance at the beginning of the year	1,000	612
Impairment loss recognised during the year	541	433
Reversal of impairment loss recognised in respect of other receivables	(217)	(45)
Balance at the end of the year	1,324	1,000

The reversal of impairment loss recognised due to the recovery of other receivables during the year.

In determining the recoverability of other receivables, the Group considers any change in the credit quality of the other receivables. Included in the provision for impairment loss recognised in respect of other receivables are individually impaired other receivables with a balance of approximately RMB1,324,000 (2008: RMB1,000,000) which have been in financial difficulty. The impairment recognised represents the difference between the carrying amount of these other receivables and the present value of the expected recoverable amounts. The Group does not hold any collateral over these balances.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2009

27. OTHER RECEIVABLES, DEPOSITS AND PREPAYMENTS (Continued)

The Company

	2009 RMB'000	2008 RMB'000
Other receivables and deposits	4,347	4,912
Prepayments (Note)	84,186	33,600
	88,533	38,512
Less: Provision for impairment loss recognised in respect of other receivables	(1,324)	(1,000)
	87,209	37,512

Note:

Prepayments mainly comprised of prepayment of value-added tax, acquisition of raw materials, packing materials and consumables, and acquisition of prepaid lease payments of approximately RMB16,012,000 (2008: RMB15,664,000), RMB52,367,000 (2008: RMB8,988,000) and RMB10,023,000 (2008: RMB5,000,000) respectively.

Movements in the provision for impairment loss recognised in respect of other receivables are as follows:

	2009 RMB'000	2008 RMB'000
Balance at the beginning of the year	1,000	612
Impairment loss recognised during the year	541	433
Reversal of impairment loss recognised in respect of other receivables	(217)	(45)
Balance at the end of the year	1,324	1,000

The reversal of impairment loss recognised due to the recovery of other receivables during the year.

In determining the recoverability of other receivables, the Company considers any change in the credit quality of the other receivables. Included in the provision for impairment loss recognised in respect of other receivables are individually impaired other receivables with a balance of approximately RMB1,324,000 (2008: RMB1,000,000) which have been in financial difficulty. The impairment recognised represents the difference between the carrying amount of these other receivables and the present value of the expected recoverable amounts. The Company does not hold any collateral over these balances.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2009

28. PLEDGED BANK DEPOSITS/CASH AND BANK BALANCES

The Group and the Company

As at 31 December 2009, bank deposits of approximately RMB237,194,000 (2008: RMB14,840,000) are pledged as collateral for bills payables.

The annual effective interest rate on pledged bank deposits is 1.98% (2008: 3.78%).

Cash and cash equivalents of the Group and the Company are denominated in RMB and HKD and bank deposits are placed with banks in the PRC and in Hong Kong. The remittance of funds out of the PRC is subject to the exchange control restrictions imposed by the PRC government.

29. TRADE AND BILLS PAYABLES

The Group and the Company

	2009 RMB'000	2008 RMB'000
Trade payables	92,013	51,014
Bills payables	236,982	14,840
	328,995	65,854

The following is an analysis of trade and bills payables by age based on the invoice date:

	2009 RMB'000	2008 RMB'000
1 to 90 days	69,664	22,160
91 to 180 days	243,286	31,662
181 to 365 days	8,624	7,469
Over 365 days	7,421	4,563
	328,995	65,854

Trade and bills payables as at 31 December 2009 and 2008 are denominated in RMB.

The average credit period on trade and bills payables is 3 months. Bills payables are all due to mature within 180 days. The Group has financial risk management policies in place to ensure that all payables are paid within the credit timeframe.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2009

30. OTHER PAYABLES AND ACCRUALS

The Group and the Company

	2009 RMB'000	2008 RMB'000
Accruals	**16,373**	9,473
Other payables	**44,901**	40,256
Received in advance (Note)	**31,020**	37,919
	92,294	87,648

Note:

As at 31 December 2008, amounts of approximately RMB21,629,000 and RMB110,000 are received in advance from a shareholder and a related company respectively (Note 37).

31. DEFERRED INCOME

The Group and the Company

During the years ended 31 December 2002 and 2003, the Company received government subsidies in cash of RMB20,380,000 pursuant to an approval obtained from the local government authority. The grants were to enable the Company to construct a new manufacturing plant to produce Chinese medicines. As at 31 December 2009, the Company has not commenced the construction of the new manufacturing plant.

32. SHARE CAPITAL

The Company

	Number of shares '000	Nominal value Domestic shares RMB'000	H shares RMB'000	Total RMB'000
Registered, issued and fully paid:				
At 31 December 2008 (nominal value of RMB0.10 each)	609,600	44,504	16,456	60,960
At 31 December 2009 **(nominal value of RMB0.10 each)**	**609,600**	**44,504**	**16,456**	**60,960**

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2009

33. RESERVES

The Group

The amounts of the Group's reserves and the movements therein for the current and prior years are presented in the consolidated statement of changes in equity to the consolidated financial statements.

The Company

The movements of reserves of the Company are as follows:

	Share premium	Statutory surplus reserve fund	Statutory public welfare fund	Retained earnings	Total
	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000
		(Note (i))	(Note (ii))		
At 1 January 2008	31,139	30,303	6,033	192,817	260,292
Profit attributable to owners of the Company	–	–	–	183,155	183,155
Transfer from retained earnings to statutory surplus reserve fund	–	177	–	(177)	–
Dividend paid	–	–	–	(12,192)	(12,192)
At 31 December 2008 and 1 January 2009	31,139	30,480	6,033	363,603	431,255
Profit attributable to owners of the Company	–	–	–	268,550	268,550
Dividend paid	–	–	–	(12,192)	(12,192)
At 31 December 2009	**31,139**	**30,480**	**6,033**	**619,961**	**687,613**

Representing:	
Proposed 2009 final dividends	12,192
Others	607,769
Retained earnings as at 31 December 2009	619,961

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2009

33. RESERVES (Continued)

Notes:

(i) Pursuant to the PRC regulations and the Company's Articles of Association, the Company is required to transfer 10% of its net profit, as determined under the PRC accounting regulations, to statutory surplus reserve fund until the fund aggregates to 50% of the Company's registered capital. The transfer to this reserve must be made before distribution of dividends to shareholders. The statutory surplus reserve fund has reached 50% of the Company's registered capital, therefore, no appropriation has been made for the year ended 31 December 2009 (2008: RMB177,000).

The statutory surplus reserve fund shall only be used to make good previous years' losses, to expand the Company's production operations, or to increase the capital of the Company. Upon approval by a resolution passed at a shareholders' general meeting, the Company may transform its statutory surplus reserve fund into share capital and issue bonus shares to existing shareholders in proportion to their original shareholdings or to increase the nominal value of each share currently held by them, provided that the balance of the reserve fund after such issue is not less than 25% of the registered capital.

(ii) Pursuant to the PRC regulations and the Company's Articles of Association, the contribution to statutory public welfare fund by the Company is voluntary. This fund can only be used to provide staff welfare facilities and other collective benefits to the Company's employees. This fund is non-distributable other than in liquidation. The directors consider that no provision to be made for the years ended 31 December 2009 and 2008.

34. BUSINESS COMBINATION

On 30 December 2009, the Company acquired 51% of the paid up capital of Sichuan Luoxin. The consideration for the acquisition was RMB459,000 which represented the cash paid as at the date of acquisition. The amount of goodwill arising as a result of the acquisition was approximately RMB165,000.

The net assets acquired in the transaction are as follows:

	The carrying amount of the acquiree's net assets before combination and at fair values
	RMB'000
Net assets acquired:	
Property, plant and equipment	5
Other receivables	540
Cash and cash equivalents	31
100% equity interest of Sichuan Luoxin	576
Minority interests	(282)
51% equity interest of Sichuan Luoxin	294
Goodwill	165
	459

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2009

34. BUSINESS COMBINATION (Continued)

	RMB'000
Total consideration satisfied by:	
Cash consideration	459
Net cash outflow arising on acquisition:	
Cash consideration	(459)
Cash and cash equivalents acquired	31
	(428)

Notes:

(i) Goodwill arose in the business combination because the cost of the combination effectively included amounts in relation to the benefit of synergies, revenue growth and future market development of Sichuan Luoxin. These benefits are not recognised separately from goodwill as the future economic benefits arising from them cannot be reliably measured.

(ii) Sichuan Luoxin did not contribute any to the Group's turnover and profit for the period from the date of acquisition to the end of the reporting period.

If the acquisition had been completed on 1 January 2009, total Group revenue for the year would have been approximately RMB907,453,000, and profit for the year attributable to owners of the Company would have been approximately RMB268,550,000. The pro forma information is for illustrative purpose only and is not necessarily an indication of revenue and results of the Group that actually would have been achieved had the acquisition been completed on 1 January 2009, nor is it intended to be a projection of future results.

35. BANKING FACILITIES

The Group had aggregate banking facilities of approximately RMB236,982,000 (2008: RMB14,840,000) which were fully utilised as at 31 December 2009.

As at 31 December 2009, RMB236,982,000 (2008: RMB14,840,000) of the banking facilities were secured by pledged bank deposits of approximately RMB237,194,000 (2008: RMB14,840,000).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2009

36. COMMITMENTS

The Group had the following significant capital commitments:

	2009 RMB'000	2008 RMB'000
Contracted but not provided for:		
– Purchase of technical know-how	3,130	3,900
– Purchase of prepaid lease payments	–	3,300
– Purchase of property, plant and equipment	10,019	–

37. RELATED PARTY TRANSACTIONS

Key management compensation for the year ended 31 December 2009 and 2008 was disclosed in Note 14(i).

Apart from those as disclosed under Notes 26 and 30 and elsewhere in the consolidated financial statements, the Group had the following material transactions with related parties during the year:

	2009 RMB'000	2008 RMB'000
Sales of finished goods to Luoxin Pharmacy Group Company Limited (previously known as Linyi Luoxin Pharmacy Company Limited) ("Luoxin Pharmacy Group") (note (i))	119,688	56,890
Sales of finished goods to The Linyi City People's Hospital ("Linyi People Hospital") (note (ii))	15,671	13,610
Sales of finished goods to The Pingyi County People's Hospital ("Pingyi People Hospital") (note (iii))	98	1,319

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2009

37. RELATED PARTY TRANSACTIONS (Continued)

Notes:

(i) Luoxin Pharmacy Group is the shareholder and promoter of the Company. Mr. Liu Baoqi is the Director for both Luoxin Pharmacy Group and the Company. As at 31 December 2009, amount of approximately RMB6,977,000 due from Luoxin Pharmacy Group is included in trade and bills receivables, the terms of the outstanding balance is set out in Note 26. As at 31 December 2008, amount of approximately RMB21,629,000 received in advance from Luoxin Pharmacy Group is included in other payables and accruals (Note 30).

(ii) Linyi People Hospital is the ex-shareholder and promoter of the Company. Mr. Yin Chuangui, a non-executive Director of the Company, is also the director of Linyi People Hospital during the year ended 31 December 2009. As at 31 December 2009, amount of approximately RMB673,000 (2008: RMB7,034,000) due from Linyi People Hospital is included in trade and bills receivables, the terms of the outstanding balance is set out in Note 26.

(iii) Pingyi People Hospital is the ex-shareholder and promoter of the Company. Mr. Liu Yuxin, a non-executive Director of the Company, is also the director of Pingyi People Hospital during the year ended 31 December 2009. As at 31 December 2008, amount of approximately RMB110,000 received in advance from Pingyi People Hospital is included in other payables and accruals (Note 30).

The above transactions constitute connected transactions under GEM Listing Rules. Please also refer to "Connected Transactions and Continuing Connected Transactions" under "Report of the Directors".

38. CONTINGENT LIABILITIES

The Group and the Company had no material contingent liabilities as at 31 December 2009.

39. SUBSEQUENT EVENTS

(a) The Company has established a sponsored American Depository Receipt ("ADR") facility with the Bank of New York Mellon. The ADRs commence trading on OTCQX under the symbol of "SLUXY" on 21 January 2010 (United States Eastern Standard Time). An ADR represents 10 ordinary shares of the Company. The ADRs are issued against ordinary shares trading on the GEM Board of the Stock Exchange that have been deposited with a custodian bank under the facility. The ADRs are traded in the United States over-the-counter market.

(b) On 22 December 2009, the Company entered into the following framework agreement with four parties.

Under Framework Agreement One, the Company shall sell chemical medicines to Luoxin Pharmacy Group for three years ending 31 December 2012. Luoxin Pharmacy Group is the single largest and a controlling shareholder of the Company and promoter of the Company. Framework Agreement One shall take effect from 1 January 2010 and expiring on 31 December 2012. The aggregate value of sales of chemical medicines to Luoxin Pharmacy Group for each of the year ending 31 December 2010, 2011 and 2012 will not exceed RMB200,000,000, RMB300,000,000 and RMB400,000,000 respectively.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2009

39. SUBSEQUENT EVENTS (Continued)

(b) (Continued)

Under Framework Agreement Two, the Company shall sell chemical medicines to Linyi People Hospital for three years ending 31 December 2012. Linyi People Hospital is the promoter of the Company. Framework Agreement Two shall take effect from 1 January 2010 and expiring on 31 December 2012. The aggregate value of sales of chemical medicines to Linyi People Hospital for each of the year ending 31 December 2010, 2011 and 2012 will not exceed RMB25,000,000, RMB30,000,000 and RMB39,000,000 respectively.

Under Framework Agreement Three, the Company shall sell chemical medicines to Shandong Luosheng Pharmacy Co., Ltd. ("Shandong Luosheng") for three years ending 31 December 2012. Shandong Luosheng is the fellow subsidiaries, of which Luoxin Pharmacy Group is holding of 51% of the equity interests of Shandong Luosheng. Framework Agreement Three shall take effect from 1 January 2010 and expiring on 31 December 2012. The aggregate value of sales of chemical medicines to Shandong Luosheng for each of the year ending 31 December 2010, 2011 and 2012 will not exceed RMB60,000,000, RMB80,000,000 and RMB100,000,000 respectively.

Under Framework Agreement Four, the Company shall sell chemical medicines to Shandong Mingxin Pharmacy Co., Ltd. ("Shandong Mingxin") for three years ending 31 December 2012. Shandong Mingxin is the fellow subsidiaries, of which Luoxin Pharmacy Group is holding of 51% of the equity interests of Shandong Mingxin. Framework Agreement Four shall take effect from 1 January 2010 and expiring on 31 December 2012. The aggregate value of sales of chemical medicines to Shandong Mingxin for each of the year ending 31 December 2010, 2011 and 2012 will not exceed RMB55,000,000, RMB75,000,000 and RMB90,000,000 respectively.

40. APPROVAL OF THE CONSOLIDATED FINANCIAL STATEMENTS

The consolidated financial statements were approved and authorised for issue by the Board of Directors on 23 March 2010.

FIVE YEARS FINANCIAL SUMMARY

	For the year ended 31 December				
	2009	2008	2007	2006	2005
	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000
Results					
Turnover	**907,453**	667,792	509,092	317,868	249,689
Cost of sales	**(479,736)**	(351,196)	(260,628)	(175,905)	(144,289)
Gross profit	**427,717**	316,596	248,464	141,963	105,400
Other revenue	**3,767**	2,613	3,323	2,565	1,548
Other income	**2,501**	2,894	2,368	2,961	–
Selling and distribution expenses	**(79,668)**	(48,869)	(33,585)	(23,637)	(21,879)
General and administrative expenses	**(42,874)**	(29,438)	(33,057)	(24,955)	(21,511)
Share of profit of an associate	**4,063**	3,107	–	–	–
Finance costs	**(240)**	(1,250)	(4,554)	(7,679)	(7,142)
Profit before taxation	**315,266**	245,653	182,959	91,218	56,416
Taxation	**(46,716)**	(62,498)	(61,016)	(31,049)	(19,486)
Profit for the year	**268,550**	183,155	121,943	60,169	36,930
Profit attributable to:					
Owners of the Company	**268,550**	183,155	121,943	60,169	36,930
Minority interests	**–**	–	–	–	–
	268,550	183,155	121,943	60,169	36,930
Dividends	**12,192**	12,192	12,192	12,192	48,182
Earnings per share attributable to owners of the Company (RMB)	**0.441**	0.300	0.200	0.099	0.079

FIVE YEARS FINANCIAL SUMMARY

	As at 31 December				
	2009	2008	2007	2006	2005
	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000
Assets & Liabilities					
Total assets	**1,220,473**	681,722	470,569	398,923	353,210
Total liabilities	**(471,618)**	(189,507)	(149,317)	(187,422)	(189,686)
	748,855	492,215	321,252	211,501	163,524
Equity attributable to owners of the Company	**748,573**	492,215	321,252	211,501	163,524
Minority interests	**282**	–	–	–	–
	748,855	492,215	321,252	211,501	163,524