# 山東羅欣藥業股份有限公司

# Shandong Luoxin Pharmacy Stock Co., Ltd.*

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

Stock Code: 8058

## INTERIM REPORT 2011

* For identification purposes only

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

**GEM has been positioned as a market designed to accommodate companies to which a higher investment risk may be attached than other companies listed on the Stock Exchange. Prospective investors should be aware of the potential risks of investing in such companies and should make the decision to invest only after due and careful consideration. The greater risk profile and other characteristics of GEM mean that it is a market more suited to professional and other sophisticated investors.**

**Given the emerging nature of companies listed on GEM, there is a risk that securities traded on GEM may be more susceptible to high market volatility than securities traded on the Main Board and no assurance is given that there will be a liquid market in the securities traded on GEM.**



*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 the information contained in this report is accurate and complete in all material respects and not misleading or deceptive, and there are no other matters the omission of which would make any statement herein or this report misleading.*

## SUMMARY

- The Group's sales for the six months ended 30 June 2011 was approximately RMB780,772,000, representing an increase of 30.38% when compared with that of the corresponding period of last year.

- The Group's profit attributable to owners of the Company for the six months ended 30 June 2011 was approximately RMB230,879,000, representing an increase of 20.22% when compared with that of the corresponding period of last year.

- The Board does not recommend the payment of any interim dividend for the six months ended 30 June 2011.

# UNAUDITED INTERIM RESULTS FOR THE SIX MONTHS ENDED 30 JUNE 2011

The board of Directors (the "Board") of the Company is pleased to announce the unaudited condensed consolidated interim report of the Company and its subsidiaries (the "Group") for the six months ended 30 June 2011 (the "Period") and the comparative figures of the corresponding period of 2010 as follows:

# CONDENSED CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

*For the six months ended 30 June 2011*

| | | Unaudited Three months ended 30 June | | Unaudited Six months ended 30 June | |
|---|---|---|---|---|---|
| | | **2011** | 2010 | **2011** | 2010 |
| | Notes | **RMB'000** | RMB'000 | **RMB'000** | RMB'000 |
| Turnover | 3 | **390,746** | 293,501 | **780,772** | 598,841 |
| Cost of sales | | **(155,928)** | (139,800) | **(306,964)** | (283,841) |
| Gross profit | | **234,818** | 153,701 | **473,808** | 315,000 |
| Other revenue | 3 | **1,840** | 2,108 | **2,861** | 3,212 |
| Other income | | **1,628** | 3,490 | **4,379** | 4,197 |
| Selling and distribution expenses | | **(105,974)** | (47,962) | **(186,985)** | (75,657) |
| General and administrative expenses | | **(13,377)** | (11,968) | **(27,617)** | (21,788) |
| Share of profit of an associate | | **2,429** | 304 | **5,265** | 588 |
| Finance costs | 4 | **–** | – | **–** | – |
| Profit before taxation | 5 | **121,364** | 99,673 | **271,711** | 225,552 |
| Taxation | 6 | **(17,989)** | (14,886) | **(40,765)** | (33,732) |
| Profit for the Period | | **103,375** | 84,787 | **230,946** | 191,820 |
| Other comprehensive income for the Period, net of tax | | **–** | – | **–** | – |
| Total comprehensive income for the Period | | **103,375** | 84,787 | **230,946** | 191,820 |

| | Notes | Unaudited Three months ended 30 June 2011 RMB'000 | Unaudited Three months ended 30 June 2010 RMB'000 | Unaudited Six months ended 30 June 2011 RMB'000 | Unaudited Six months ended 30 June 2010 RMB'000 |
|---|---|---|---|---|---|
| Profit attributable to: | | | | | |
| Owners of the Company | | **103,245** | 84,995 | **230,879** | 192,050 |
| Non-controlling interests | | **130** | (208) | **67** | (230) |
| | | **103,375** | 84,787 | **230,946** | 191,820 |
| Total comprehensive income attributable to: | | | | | |
| Owners of the Company | | **103,245** | 84,995 | **230,879** | 192,050 |
| Non-controlling interests | | **130** | (208) | **67** | (230) |
| | | **103,375** | 84,787 | **230,946** | 191,820 |
| Earnings per share attributable to owners of the Company (RMB) | | | | | |
| – Basic and diluted | 8 | **16.94 cents** | 13.94 cents | **37.87 cents** | 31.50 cents |

# CONDENSED CONSOLIDATED STATEMENT OF FINANCIAL POSITION

*As at 30 June 2011*

| | Notes | Unaudited 30 June 2011 RMB'000 | Audited 31 December 2010 RMB'000 |
|---|---|---|---|
| **Non-current assets** | | | |
| Interest in an associate | | 24,917 | 25,051 |
| Available-for-sale financial assets | | 1,000 | 1,000 |
| Purchased technical know-how | 9 | 1,192 | 1,202 |
| Prepayments to acquire technical know-how | | 7,520 | 7,520 |
| Property, plant and equipment | 10 | 266,864 | 268,270 |
| Construction-in-progress | | 83,279 | 52,826 |
| Prepaid lease payments | 11 | 19,853 | 20,101 |
| Deferred tax assets | | 3,512 | 3,512 |
| Goodwill | | 165 | 165 |
| | | 408,302 | 379,647 |
| **Current assets** | | | |
| Inventories | | 168,707 | 215,389 |
| Trade and bills receivables | 12 | 228,969 | 222,922 |
| Other receivables, deposits and prepayments | | 97,803 | 79,101 |
| Pledged bank deposits | | 11,190 | 91,837 |
| Cash and bank balances | | 783,358 | 582,010 |
| | | 1,290,027 | 1,191,259 |
| **Current liabilities** | | | |
| Trade and bills payables | 13 | 94,599 | 184,348 |
| Other payables and accruals | | 177,835 | 170,182 |
| Deposits received | | 23,201 | 22,343 |
| Dividend payable | | 9,720 | 8,757 |
| Taxation payable | | 49,202 | 41,970 |
| | | 354,557 | 427,600 |

| | Notes | Unaudited 30 June 2011 RMB'000 | Audited 31 December 2010 RMB'000 |
|---|---|---|---|
| **Net current assets** | | **935,470** | 763,659 |
| **Total assets less current liabilities** | | **1,343,772** | 1,143,306 |
| **Non-current liability** | | | |
| Deferred income | | **20,380** | 20,380 |
| **Net assets** | | **1,323,392** | 1,122,926 |
| **Capital and reserves** | | | |
| Share capital | 14 | **60,960** | 60,960 |
| Reserves | | **1,260,831** | 1,060,432 |
| Equity attributable to owners of the Company | | **1,321,791** | 1,121,392 |
| Non-controlling interests | | **1,601** | 1,534 |
| | | **1,323,392** | 1,122,926 |

# CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

*For the six months ended 30 June 2011*

| | Share capital RMB'000 | Share premium RMB'000 | Statutory surplus reserve fund RMB'000 | Statutory public welfare fund RMB'000 | Retained earnings RMB'000 | Attributable to owners of the Company RMB'000 | Non-controlling interests RMB'000 | Total RMB'000 |
|---|---|---|---|---|---|---|---|---|
| At 1 January 2011, audited | 60,960 | 31,139 | 30,493 | 6,033 | 992,767 | 1,121,392 | 1,534 | 1,122,926 |
| Total comprehensive income | – | – | – | – | 230,879 | 230,879 | 67 | 230,946 |
| Dividend declared | – | – | – | – | (30,480) | (30,480) | – | (30,480) |
| At 30 June 2011, unaudited | 60,960 | 31,139 | 30,493 | 6,033 | 1,193,166 | 1,321,791 | 1,601 | 1,323,392 |

*For the six months ended 30 June 2010*

| | Share capital RMB'000 | Share premium RMB'000 | Statutory surplus reserve fund RMB'000 | Statutory public welfare fund RMB'000 | Retained earnings RMB'000 | Attributable to owners of the Company RMB'000 | Non-controlling interests RMB'000 | Total RMB'000 |
|---|---|---|---|---|---|---|---|---|
| At 1 January 2010, audited | 60,960 | 31,139 | 30,480 | 6,033 | 619,961 | 748,573 | 282 | 748,855 |
| Total comprehensive income | – | – | – | – | 192,050 | 192,050 | (230) | 191,820 |
| Dividend declared | – | – | – | – | (12,192) | (12,192) | – | (12,192) |
| Addition to non-controlling interests due to additional capital injection to a subsidiary | – | – | – | – | – | – | 980 | 980 |
| At 30 June 2010, unaudited | 60,960 | 31,139 | 30,480 | 6,033 | 799,819 | 928,431 | 1,032 | 929,463 |

# CONDENSED CONSOLIDATED STATEMENT OF CASH FLOWS

*For the six months ended 30 June 2011*

| | Unaudited six months ended 30 June | |
|---|---|---|
| | **2011** | 2010 |
| | **RMB'000** | RMB'000 |
| Net cash inflow from operating activities | **183,677** | 83,723 |
| Net cash outflow from investing activities | **(33,459)** | (22,510) |
| Net cash inflow from financing activities | **51,130** | 137,510 |
| Net increase in cash and cash equivalents | **201,348** | 198,723 |
| Cash and cash equivalents at beginning of Period, audited | **582,010** | 263,749 |
| Cash and cash equivalents at end of Period, unaudited | **783,358** | 462,472 |
| Analysis of the balances of cash and cash equivalents Cash and bank balances | **783,358** | 462,472 |

# NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS

*For the six months ended 30 June 2011*

## 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 liabilities company with a registered capital of Renminbi ("RMB") 46 million. 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 GEM of 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 selling 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 accounts have been approved for issue by the Board on 9 August 2011.

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The unaudited condensed consolidated interim financial statements have been prepared in accordance with the Hong Kong Accounting Standard ("HKAS") 34 "Interim Financial Reporting" issued by the Hong Kong Institute of Certified Public Accountants ("HKICPA") and the disclosure requirements set out in Chapter 18 of the GEM Listing Rules. The accounting policies adopted are consistent with those followed in the preparation of the Company's audited consolidated financial statements for the year ended 31 December 2010.

The consolidated financial statements have been prepared under historical cost basis except for certain financial assets and financial liabilities, which are measured at fair values.

## 3. TURNOVER AND OTHER REVENUE

The Group currently operates in one business segment in the manufacturing and selling 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 reported to the chief operating decision makers are the net profits of the Group and the reportable assets and liabilities reported to the chief operating decision makers are the Group's assets and liabilities. Accordingly, the Group does not have separately reportable segment.

Turnover and other revenue recognised are as follows:

| | **Unaudited Six months ended 30 June** | |
|---|---|---|
| | **2011 RMB'000** | 2010 RMB'000 |
| **Turnover** | | |
| Sales of manufactured pharmaceutical products | **780,772** | 598,841 |
| **Other revenue** | | |
| Interest income | **2,861** | 3,212 |
| **Total revenue** | **783,633** | 602,053 |

## 4. FINANCE COSTS

| | **Unaudited Six months ended 30 June** | |
|---|---|---|
| | **2011 RMB'000** | 2010 RMB'000 |
| Bank loans wholly repayable within five years | **–** | – |

## 5. PROFIT FROM OPERATIONS

| | Unaudited Six months ended 30 June | |
|---|---|---|
| | **2011** | 2010 |
| | **RMB'000** | RMB'000 |
| Operating profit of the Group was determined after charging/(crediting) the following: | | |
| Directors' and supervisors' emoluments | **769** | 585 |
| Depreciation of property, plant and equipment | **10,747** | 9,847 |
| Loss on disposal of property, plant and equipment | **–** | 1 |
| Amortisation of prepaid lease payments | **248** | 158 |
| Amortisation of purchased technical know-how (included in cost of sales) | **10** | 472 |
| Employees benefit expenses (excluding Directors' and supervisors' emoluments) | **77,006** | 14,160 |
| Research and development costs | **7,900** | 6,656 |
| Advertising costs | **3,724** | 2,822 |

## 6. TAXATION

| | Unaudited Six months ended 30 June | |
|---|---|---|
| | **2011** | 2010 |
| | **RMB'000** | RMB'000 |
| PRC enterprise income tax | **40,765** | 33,732 |

No provision for Hong Kong profits tax has been made as the Group did not carry out any business in Hong Kong during the Period.

## 7. DIVIDENDS

The Board does not recommend the payment of any interim dividend for the Period (2010: Nil).

## 8. EARNINGS PER SHARE

The calculation of basic earnings per share for the six months ended 30 June 2011 is based on the unaudited net profit of approximately RMB230,879,000 and the weighted average number of approximately 609,600,000 ordinary shares in issue during the Period.

The calculation of basic earnings per share for the six months ended 30 June 2010 is based on the unaudited net profit of approximately RMB192,050,000 and the weighted average number of approximately 609,600,000 ordinary shares in issue during the period.

Diluted earnings per share is the same as the basic earnings per share since there were no dilutive events existed during the period ended 30 June 2011 and 2010.

## 9. PURCHASED TECHNICAL KNOW-HOW

| | RMB'000 |
|---|---|
| **Cost:** | |
| At 1 January 2010, audited | 17,450 |
| Additions | – |
| At 31 December 2010 and 1 January 2011, audited | 17,450 |
| Additions | – |
| At 30 June 2011, unaudited | 17,450 |
| **Accumulated amortisation and impairment:** | |
| At 1 January 2010, audited | 15,454 |
| Charge for the year | 794 |
| At 31 December 2010 and 1 January 2011, audited | 16,248 |
| Charge for the Period | 10 |
| At 30 June 2010, unaudited | 16,258 |
| **Net book value:** | |
| **At 30 June 2011, unaudited** | **1,192** |
| At 31 December 2010, audited | 1,202 |

## 10. PROPERTY, PLANT AND EQUIPMENT

| | RMB'000 |
|---|---|
| **Cost:** | |
| At 1 January 2010, audited | 317,651 |
| Additions | 15,231 |
| Transfer from construction-in-progress | 12,934 |
| Disposals | (772) |
| At 31 December 2010 and 1 January 2011, audited | 345,044 |
| Additions | 9,341 |
| At 30 June 2011, unaudited | 354,385 |
| **Accumulated depreciation and impairment:** | |
| At 1 January 2010, audited | 57,430 |
| Charge for the year | 19,822 |
| Written back on disposals | (478) |
| At 31 December 2010 and 1 January 2011, audited | 76,774 |
| Charge for the Period | 10,747 |
| At 30 June 2011, unaudited | 87,521 |
| **Net book value:** | |
| **At 30 June 2011, unaudited** | **266,864** |
| At 31 December 2010, audited | 268,270 |

As at 30 June 2011, all buildings of the Group are located in the PRC.

Depreciation expense of RMB7,551,000 (six months ended 30 June 2010: RMB6,590,000) have been expensed in cost of sales and RMB3,196,000 (six months ended 30 June 2010: RMB3,257,000) have been included in administrative expenses for the Period.

## 11. PREPAID LEASE PAYMENTS

Prepaid lease payments represent 50-year to 70-year land use rights in the PRC expiring from November 2050 to September 2079. This payment is recognised as an expense over the leasehold period.

| | RMB'000 |
|---|---|
| At 1 January 2010, audited | 11,174 |
| Additions | 9,717 |
| Amortisation of prepaid lease payments | (378) |
| At 31 December 2010 and 1 January 2011, audited | 20,513 |
| Amortisation of prepaid lease payments | (248) |
| **At 30 June 2011, unaudited** | 20,265 |

Analysed for reporting purposes as:

| | **At 30 June 2011 RMB'000 (Unaudited)** | At 31 December 2010 RMB'000 (Audited) |
|---|---|---|
| Current assets (included in other receivables, deposits and prepayments) | **412** | 412 |
| Non-current assets | **19,853** | 20,101 |
| | **20,265** | 20,513 |

The Group's prepaid lease payments comprise:

| | **At 30 June 2011 RMB'000 (Unaudited)** | At 31 December 2010 RMB'000 (Audited) |
|---|---|---|
| Land in PRC | | |
| Long lease | **9,544** | 9,613 |
| Medium-term lease | **10,763** | 10,900 |
| | **20,307** | 20,513 |

## 12. TRADE AND BILLS RECEIVABLES

Details of the ageing analysis are as follows:

| | At 30 June 2011 RMB'000 (Unaudited) | At 31 December 2010 RMB'000 (Audited) |
|---|---|---|
| 1 to 90 days | 141,100 | 189,120 |
| 91 to 180 days | 36,803 | 32,032 |
| 181 to 365 days | 51,066 | 1,770 |
| Over 365 days | 7,929 | 7,199 |
| | 236,898 | 230,121 |
| Less: Provision of impairment loss recognised in respect of trade receivables | (7,929) | (7,199) |
| | 228,969 | 222,922 |

Customers are generally granted with credit term of 180 days.

Trade and bills receivables as at 30 June 2011 are denominated in RMB.

## 13. TRADE AND BILLS PAYABLES

Details of the ageing analysis are as follows:

| | At 30 June 2011 RMB'000 (Unaudited) | At 31 December 2010 RMB'000 (Audited) |
|---|---|---|
| 1 to 90 days | 56,473 | 74,311 |
| 91 to 180 days | 19,468 | 92,742 |
| 181 to 365 days | 5,333 | 2,332 |
| Over 365 days | 13,325 | 14,963 |
| | 94,599 | 184,348 |

Trade and bills payables as at 30 June 2011 are denominated in RMB.

## 14. SHARE CAPITAL

| | | Nominal value | | |
|---|---|---|---|---|
| | **Number of shares** | **Domestic shares** | **H shares** | **Total** |
| | '000 | RMB'000 | RMB'000 | RMB'000 |
| At 31 December 2010, audited (nominal value of RMB0.10 each) | 609,600 | 44,504 | 16,456 | 60,960 |
| **At 30 June 2011, unaudited (nominal value of RMB0.10 each)** | 609,600 | 44,504 | 16,456 | 60,960 |

## 15. BANKING FACILITIES

As at 30 June 2011, the Company had aggregate banking facilities of RMB11,190,000 (as at 31 December 2010: RMB86,837,000) which were fully utilised as at 30 June 2011.

As at 30 June 2011, approximately RMB11,190,000 (as at 31 December 2010: RMB86,837,000) of the banking facilities were secured by pledged bank deposits of RMB11,190,000 (as at 31 December 2010: RMB91,837,000).

## 16. COMMITMENTS

As at 30 June 2011, the Group had the following significant capital commitments:

| | **At 30 June 2011 RMB'000 (Unaudited)** | At 31 December 2010 RMB'000 (Audited) |
|---|---|---|
| Contracted but not provided for: | | |
| – Purchase of technical know-how | **3,130** | 3,130 |
| – Purchase of property, plant and machinery | **84,309** | 50,905 |

## 17. RELATED PARTY TRANSACTIONS

Save as disclosed elsewhere in the interim consolidated financial statements, the Company had the following material transactions with related parties during the Period:

| | Unaudited Six months ended 30 June | |
|---|---|---|
| | **2011** | 2010 |
| | **RMB'000** | RMB'000 |
| | **(Unaudited)** | (Unaudited) |
| Sales of finished goods to Luoxin Pharmacy Group Company Limited ("Luoxin Pharmacy Group") (note (i)) | **195,346** | 91,769 |
| Sales of finished goods to Shandong Luosheng Pharmacy Co., Limited ("Shandong Luosheng") (note (ii)) | **26,762** | 23,581 |
| Sales of finished goods to Shandong Mingxin Pharmacy Co., Limited ("Shandong Mingxin") (note (iii)) | **24,396** | 16,832 |

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.

(ii) Shandong Luosheng is the fellow subsidiary, of which Luoxin Pharmacy Group is holding 51% of the equity interests of Shandong Luosheng.

(iii) Shandong Mingxin is the fellow subsidiary, of which Luoxin Pharmacy Group is holding 51% of the equity interests of Shandong Mingxin.

## 18. APPROVAL OF THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS

The interim consolidated financial statements were approved by the Board on 9 August 2011.

## DIVIDENDS

On 15 March 2011, the Board recommended the payment of a final dividend of RMB0.05 per share in respect of the year ended 31 December 2010 to shareholders whose names appear in the register of members of the Company on 2 May 2011. This proposed final dividend was approved by the shareholders of the Company at the annual general meeting which was held on 1 June 2011.

The Board does not recommend the payment of any interim dividend for the Period.

## MANAGEMENT DISCUSSION AND ANALYSIS

### *Introduction*

In 2011, with the medical reform introduced proactively by the government, further standardization and input into the pharmaceutical industry, basis public health services was improved accordingly, which in turn gradually increases the inputs into medical and health areas. Together with the expansion of medical insurance coverage, the strengthening of rural health services, the enhancement of new rural cooperative medical services, the trend of aging population, the acceleration in urbanization, and the steady growth of global pharmaceutical market, the development of pharmaceutical industry in the PRC will continue to be promising in 2011.

As a leading modern pharmaceutical enterprise in the PRC, the Group has always insisted on the strategic core competencies of enhancing its science and technology innovation, accelerating its capabilities in research and development and distribution, and consolidating its production. Best endeavours were used in the provision of reliable, high-technology and high value added pharmaceutical products. During the Period under review, the Group fully leveraged on the opportunities arising from the expansion in the market and fulfilled market demand by investing additional resources in enhancing production capabilities and technologies and accelerating the research and development of new products. At the same time, the Group has been keen on tapping into a broader market in order to increase its market share. This in turn will allow satisfactory growth in both turnover and earnings, building a solid foundation for the sustainable development of the Group in future.

### *Business Review*

For the six months ended 30 June 2011, the Group has been consistent in implementing the development strategies as formulated earlier and the targets of the Twelfth Five-Year Plan. A sound condition in operation has thus been sustained in the first year of the Twelfth Five-Year Plan. Hence, the profit attributable to shareholders of the Group recorded remarkable growth compared to the same period of the last year. There had been strong momentum driving the growth of the Group. The outstanding results were attributable to the support and cooperation of all shareholders, customers, suppliers, business partners and the public, as well as the concerted and unremitting efforts of the management and staff of the Group. By capitalizing the successes already achieved, the Group will further strengthen its research and development capacities and expand its market network to further enhance its brand recognition and competitiveness so as to build up a world-class pharmaceutical brand.

### *Research and Development*

1. *Building a platform for technology research and development*

   Prior to the Period under review, the Group has been recognised as an "Industrial Model Enterprise in the National Integrated Platform for New Pharmaceutical Research, Development and Technology (Shandong)" (國家綜合性新藥研發技術大平台(山東)產業化示範企業) and "Key High-Tech Enterprise under the State Torch Program" (國家火炬計劃重點高新技術企業). The Group has also established the "Post-Doctoral Research Workshop of the State" (國家博士後科研工作站). On such basis, during the Period under review, the Group was allowed to establish "Shandong Key Lyophilized Powder Injection Pharmaceutical Laboratory", "Shandong Key Lyophilized Powder Injection Pharmaceutical Engineering Laboratory" and the position of "Taishan Scholar – Pharmaceutical expert consultant", so as to introduce talents and build a stronger platform of research and development and technology improvement for the Group, which will further strengthen the research and development competencies of the Group and enhance its overall competitiveness.

2. *New products and patents*

   During the Period under review, the Group received 15 patents of invention in the PRC. It is now applying for 12 patents of invention in the PRC. Five new drugs were approved for production and registration. As of 30 June 2011, the Group had 48 patents, of which 38 were national patents.

### *Production and Management*

1. The Group continued to implement effective strategies on the seven integral parts of its operation, namely management, culture, business organization, capital operation, science and technology innovation, human resources and marketing. This had effectively contributed to the development of the Group and further enhanced its risk mitigating capabilities and overall competencies. 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. The Company was named as one of the "Top Twenty Most Competitive Listed Pharmaceutical Companies in China" by China Pharmaceutical Enterprise Management Association last year. These recognitions demonstrated the growth in the overall corporate strength of the Group.

2. *Construction of production facilities*

(1) Pharmaceutical preparations: the construction of infusion workshop and ancillary facilities of Shandong Yuxin Pharmacy Co., Ltd. has completed, and is expected to generate revenue next year.

(2) Pharmaceutical raw materials: the construction of pharmaceutical raw materials project of Shandong Hengxin Pharmacy Co., Ltd. is underway. The first phase of the project is scheduled to be completed and ready for operation at the end of the year.

### *Sales and Marketing*

The Group continued to integrate sales resources and build up an outstanding sales team to increase the market share and competitiveness of products. At present, the Group has built an intensive and seamless sales network throughout China and has established a sound marketing management system for business solicitation and sales of hospital terminal products, OTC products, the third terminal products and pharmaceutical raw materials and logistics distribution.

### *Financial Review*

For the six months ended 30 June 2011, the Group's unaudited turnover was approximately RMB780,772,000, representing an increase of approximately 30.38% from approximately RMB598,841,000 for the corresponding period of last year. The increase was attributable to the Group'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 six months ended 30 June 2011, the unaudited cost of sales was approximately RMB306,964,000, representing an increase of 8.15% from approximately RMB283,841,000 for the corresponding period of last year.

For the six months ended 30 June 2011, the unaudited gross profit margin was 60.68%, representing an increase of 8.08% from 52.60% for the corresponding period of last year. The increase was attributable to the Company's launch of products with high added values and upgrade of product portfolio.

For the six months ended 30 June 2011, the unaudited operating expenditure was approximately RMB214,602,000, representing an increase of 120.23% from approximately RMB97,445,000 for the corresponding period of last year. The increase of operating expenditure was due to the changes in sales mix which were associated with different cost pattern of sales and marketing expenses and the increase in research and development expenses for products which might be launched in the future.

For the six months ended 30 June 2011, the unaudited profit attributable to owners of the company was approximately RMB230,879,000, representing an increase of 20.22% from approximately RMB192,050,000 for the corresponding period of last year. Weighted average earnings per share were RMB0.38 for the six months ended 30 June 2011.

### *Liquidity and Financial Resources*

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

As at 30 June 2011, the Group's cash and cash equivalents amounted to approximately RMB794,548,000 (as at 30 June 2010: RMB562,156,000). As at 30 June 2011, the Group did not have any borrowings (as at 30 June 2010: nil).

### *Pledged Bank Deposits/Cash and Cash Equivalents*

As at 30 June 2011, the Group's bank deposits amounting to approximately RMB11,190,000 were pledged as security for remittance under acceptance (as at 30 June 2010: bank deposits of approximately RMB99,684,000 were pledged as security for remittance under acceptance).

### *Major Acquisition and Disposal*

For the six months ended 30 June 2011, the Group did not have any major acquisition or disposal.

### *Significant Investment*

For the six months ended 30 June 2011, the Group did not make any significant investment.

### *Contingent Liabilities*

For the six months ended 30 June 2011, the Group did not have any substantial contingent liabilities.

### *Exchange Risk*

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

Most of the Group'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 Group and in raising its profitability. The Group 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 Group has established a remuneration committee to make recommendations on the overall strategy for remuneration policy.

### *Prospects*

Looking ahead, since the development of the pharmaceutical industry is one of the focuses of the State's policies in future, the prospects of the pharmaceutical industry is optimistic. The pharmaceutical industry has already been included as one of the industries that will be supported by the policies in the Twelfth Five-Year Plan published by the PRC central government. It is expected that the central government will allocate more resources to the pharmaceutical and medical equipment industries. A modern market system for pharmaceutical products circulation will be established during the Twelfth Five-Year Plan so as to enhance the concentration of the industry. The Group is confident to maintain its sustained development and growth.

In addition, the Guiding Opinions on Speeding up the Restructure of the Pharmaceutical Industry (the "Opinions") was jointly published by the Ministry of Industry and Information Technology, the Ministry of Health and the State Food and Drug Administration in November 2010. The aims of the Opinions were to speed up the restructure of the pharmaceutical industry, to cultivate independent innovation capacity and to enhance the concentration in production. The Opinions are beneficial to the development of innovative enterprises as a whole. This will give more room for competitive enterprises to develop.

In future, the Group will continue to pursue the strategic directions of "Technology-driven enterprise with determination and efforts" under the favourable operating environment. By fully leveraging on the opportunities arising from the integration of the pharmaceutical industry, the Group will continue to expand its investment in research and development and enhance the standards in research and development as well as technologies. This will allow the Group to invent and develop more products of higher technology, better quality and higher added value. The Group also aims at cost reduction and expansion of production scale so as to achieve economies of scale, lower cost of production and differentiation of competitive edge. As the Group has begun the construction of new plants for Yuxin and Hengxin, production capabilities will be increased to satisfy the growing demand for pharmaceutical products in the market. We can also increase the categories of pharmaceutical products and expand its scope in research and development on new drugs more effectively. This will facilitate a more comprehensive development in business. The Group will also proactively establish a broader sales network so as to enhance the market share of its products. The core competencies in the Group will thus be improved in an ongoing manner.

With the implementation of the strategies above, it is anticipated by the Group that "Luoxin" will be transformed into a brand representing world-class pharmaceutical enterprise. With the rapid growth in production capabilities and the launch of more high value added products, the Group is confident to maintain a steady growth in its business so as to bring satisfactory return to its shareholders.

## APPROVAL OF FINANCIAL STATEMENTS

The financial statements were approved by the Board on 9 August 2011.

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

As at 30 June 2011, the interests and short positions of each Director and supervisor 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, as at 30 June 2011*

| 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 | 250,639,949 | 56.32% | 41.12% |
| Mr. Liu Zhenhai (劉振海) | Beneficial Owner | 35,000,000 | 7.86% | 5.74% |

Note 1: These 250,639,949 domestic shares of the Company ("Domestic Shares") are registered in the name of Luoxin Pharmacy Group Company Limited ("Luoxin Pharmacy Group", previously known 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 250,639,949 Domestic Shares held by Luoxin Pharmacy Group. The total number of Domestic Shares deemed to be interested by Mr. Liu as at 30 June 2011 was 250,639,949 (representing 56.32% of total issued Domestic Shares and 41.12% of Company's share capital). On 29 October 2007, Luoxin Pharmacy Group further acquired 8,639,949 shares, including 4,319,974.50 Domestic Shares from each of two promoters of the Company, i.e., Linyi City People's Hospital and Pinyi County People's Hospital. On 18 January 2010, Luoxin Pharmacy Group further acquired 12,000,000 Domestic Shares from Mr. Cao Chuan (曹傳) ("Mr. Cao"), who was holding 28,640,136 Domestic Shares before this share transfer. The rest of Mr. Cao's Domestic Shares were sold to another two independent third parties on the same date.

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

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 30 June 2011, 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 30 June 2011*

| Name of director | Capacity/Nature of Interest | Number of domestic shares | % of total issued domestic shares | % of Company's share capital |
|---|---|---|---|---|
| Luoxin Pharmacy Group | Beneficial Owner | 250,639,949 | 56.32% | 41.12% |
| Zuo Hongmei (左洪梅) | Family interest (note 1) | 250,639,949 | 56.32% | 41.12% |
| 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 250,639,949 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 250,639,949 Domestic Shares held by Luoxin Pharmacy Group. Zuo Hongmei (左洪梅), as the wife of Mr. Liu, is taken to be interested in the entire 250,639,949 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 the 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 the 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 interested in less than 10% of the total registered share capital of the Company.

## AUDIT COMMITTEE

An audit committee of the Company (the "Audit Committee") was established on 20 November 2005 and its current members during the Period include:

Mr. Foo Tin Chung, Victor (傅天忠) *(Chairman)*

Mr. Fu Hongzheng (付宏征)

Ms. Li Hongjian (李宏建)

The Company has established the Audit Committee with written terms of reference in compliance with paragraph C3 of the Code on 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 of 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 unaudited results of the Company for the Period have been reviewed by the Audit Committee.

## DIRECTOR'S 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 Period.

## CORPORATE GOVERNANCE

The Board has reviewed the Company's corporate governance practices and is satisfied that the Company has complied with the Code for the Period.

## PURCHASE, SALE OR REDEMPTION OF LISTED SECURITIES

The Group has not redeemed, purchased or sold any of its listed securities during the Period.

## COMPETING BUSINESS

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

### *Luoxin Pharmacy Group*

Luoxin Pharmacy Group is the controlling shareholder of the Company which holds 41.12% of the Company's issued share capital. The chairman of the Company, Mr. Liu, 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.

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 and health and beauty products. Since the execution of the non-competition undertaking, Luoxin Pharmacy Group has undertaken to cease 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 medium-sized medical institutions, i.e. hospitals below county-level. The Company 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 sales 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 does 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 medicinal products sold by Linyi Municipal Pharmacy which have the same or similar curative effects as those of the Group may be in competition with the products of the Group.

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.

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

PRC, 9 August 2011

*As at the date of this report, the Board comprises 10 Directors, of which Mr. Liu Baoqi (劉保起), Mr. Liu Zhenhai (劉振海), Ms. Li Minghua (李明華), Mr. Han Fengsheng (韓風生) and Mr. Chen Yu (陳雨) are executive Directors, Mr. Yin Chuangui (尹傳貴) and Mr. Liu Yuxin (劉玉欣) are non-executive Directors and Mr. Foo Tin Chung, Victor (傅天忠), Mr. Fu Hongzheng (付宏征) and Ms. Li Hongjian (李宏建) are independent non-executive Directors.*

*This report will appear and remain on the GEM website at www.hkgem.com on the "Latest Company Reports" page for at least 7 days from the date of its posting and on the Company's website at: http://shandongluoxin.quamir.com/*

* *For identification purposes only*