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

ANNUAL REPORT 2012

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

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CORPORATE INFORMATION

DIRECTORS

Executive Directors

Liu Baoqi
Liu Zhenhai
Li Minghua
Han Fengsheng
Chen Yu

Non-executive Directors

Yin Chuangui
Liu Yuxin (resigned on 31 December 2012)

Independent non-executive Directors

Foo Tin Chung, Victor
Fu Hongzheng
Li Hongjian
Prof. Chen Yun Zhen (appointed on 31 December 2012)

SUPERVISORS

Sun Song
Guan Yonghua
Wan Jian
Song Liang Wei

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

MEMBERS OF THE AUDIT COMMITTEE

Foo Tin Chung, Victor *(chairman of the audit committee)*
Fu Hongzheng
Li Hongjian
Prof. Chen Yun Zhen (appointed on 31 December 2012)

LEGAL ADVISER TO THE COMPANY

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

AUDITORS

HLB Hodgson Impey Cheng Limited
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

PRINCIPAL PLACE OF BUSINESS IN HONG KONG

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

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 the Company and its subsidiaries (collectively the "Group") for the year ended 31 December 2012 (hereinafter referred to as the "year") for your review.

With an aim of maximising shareholders' value, our Company is devoted to enhancing the capabilities in research and development, increasing production capacity and consolidating sales network development, focusing on speeding up of the adjustment of product structure and production of compressed antibiotic products, expedition of market development of products for respiratory and digestive systems. The profit margins and competitiveness of our core operations improved in an ongoing manner. Through dedication and concerted efforts of the management and employees, the Company achieved rapid growth and healthy development. For the year ended 31 December 2012, turnover increased by 36.97% to RMB2,228,257,000, whereas profit attributable to shareholders increased by 3.12% to RMB439,874,000.

In the past year, we spared no efforts to implement the targets of the Twelfth Five-Year Plan. Our capabilities in, among others, management, market network development, technology development, elite team building, spiritual civilisation development, brand building and goodwill have 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, Shandong Yuxin Pharmacy Co., Ltd., a new member of the Group, has been granted the Drug Manufacturing Certificate (藥品生產許可證), and the construction of its infusion workshop and ancillary facilities was completed. Lyophilized Powder Injection workshop and solid dosage workshop (both in compliance with the new Good Manufacturing Practices ("GMP") standard of China) passed the new GMP certification. Shandong Hengxin Pharmacy Co., Ltd. is speeding up the construction of its pharmaceutical raw materials project, and the first phase of the composite materials workshop has commenced production. These projects expand the categories of new products of the Company and rapidly increase the integrated annual production capability. A number of the Company's new products were derived from the successful research and development results, which were subsequently commercialised. Tens of products received invention patents and Scientific and Technological Progress Awards granted by the State. Before the year under review, the Group has established or 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), a "National Post-Doctoral Research Workshop" (國家博士後科研工作站) and "Key High-Tech Enterprise under the State Torch Program" (國家火炬計劃重點高新技術企業). On such basis, the Group has also been permitted to establish the "Shandong Key Lyophilized Powder Injection Pharmaceutical Laboratory" (山東省凍乾粉針劑藥物重點實驗室), the "Shandong Key Lyophilized Powder Injection Pharmaceutical Engineering Laboratory" (山東省凍乾粉針劑藥物工程實驗室), the position of "Taishan Scholar – Pharmaceutical expert consultant" (泰山學者－藥學特聘專家) and the "Enterprise Academician Workstation of Shandong Province" (山東省企業院士工作站). During the year under review, our Company was approved by the National Development and Reform Commission to establish a state-province joint engineering laboratory, which built a stronger platform of talent introduction and technology improvement for the Group, and which in turn strengthened the research and development capabilities. At present, the Company has an extensive and seamless sales network throughout China and a sound marketing management system, and accelerated the development of the rural market, and formed an OTC sales network, aiming to build the third terminal direct sales network.

CHAIRMAN'S STATEMENT

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 active pharmaceutical ingredients to pharmaceutical finished products in various dosage forms.

We believe that the pharmaceutical industry will maintain rapid growth in 2013. Particularly with the acceleration of the implementation of medical reform imposed by the State, the proactive introduction of new cooperative medical initiatives, further input into the pharmaceutical industry, and the improvement of public health services, together with the trends of aging population and the acceleration in urbanisation, the overall market expenses on medical and pharmaceutical treatment will increase dramatically. Such huge market potential will enable well-established enterprises to enter a new era of rapid development. China is one of the countries that consume a lot of pharmaceuticals, the room for development is extensive. The pharmaceutical industry is incorporated into the list of supported industries in the Twelfth Five-Year Plan of the PRC central government. The central government will allocate more resources to the pharmaceutical and medical equipment industries. Looking ahead to 2013, 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.

The rapid development and advancement of Luoxin Pharmacy always depends on the sustained efforts 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 our Company.

Liu Baoqi
Chairman
19 March 2013

PROFILES OF DIRECTORS, SUPERVISORS AND SENIOR MANAGEMENT

EXECUTIVE DIRECTORS

Mr. Liu Baoqi (劉保起), aged 51, 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) in 1995. 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 currently the chairman of the board of director of Luoxin Pharmacy Group, Shandong Luosheng Pharmacy Company Limited* (山東羅盛醫藥有限公司) and Shandong Mingxin Pharmacy Company Limited* (山東明欣醫藥有限公司). Mr. Liu is interested in 51.73% of the registered share capital of Luoxin Pharmacy Group. Mr. Liu is the uncle of Mr. Liu Zhenhai.

Mr. Liu Zhenhai (劉振海), aged 37, 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 15 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 Luo Zhuang District People's Congress. Mr. Liu Zhenhai is currently the director of Luoxin Pharmacy Group and Shandong Luosheng Pharmacy Company Limited* (山東羅盛醫藥有限公司), Shandong Mingxin Pharmacy Company Limited* (山東明欣醫藥有限公司) and Shandong Hengxin Pharmacy Company Limited* (山東恒欣藥業有限公司). Mr. Liu Zhenhai is the nephew of Mr. Liu Baoqi.

Ms. Li Minghua (李明華), aged 47, 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. Ms. Li was granted the Qi Lu Female Inventor award (齊魯巾幗發明家) in 2010. She was accredited as Outstanding Engineer of Shandong Province (山東省優秀工程師) in 2011 and was granted the Adutescent Professional with Outstanding Contribution of Shandong Province (山東省有突出貢獻的中青年專家). She is a delegate of the Fei County People's Congress. Ms. Li is currently a director of Shandong Yuxin Pharmacy Company Limited* (山東裕欣藥業有限公司).

PROFILES OF DIRECTORS, SUPERVISORS AND SENIOR MANAGEMENT

Mr. Han Fengsheng (韓風生), aged 37, 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. Han is a member of the National Committee of the Chinese People's Political Consultative Conference of Luo Zhuang District.

Mr. Chen Yu (陳雨), aged 44, is an executive Director and the vice general manager who is responsible for production management. 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 19 years of experience in the PRC medicine manufacturing industry.

NON-EXECUTIVE DIRECTORS

Mr. Yin Chuangui (尹傳貴), aged 56, 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 54, 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. Mr. Liu resigned as non-executive Director on 31 December 2012.

INDEPENDENT NON-EXECUTIVE DIRECTORS

Foo Tin Chung Victor (傅天忠), aged 44, 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 the Stock Exchange. Mr. Foo had served as an independent non-executive director of Hanergy Solar Group Limited (formerly known as Apollo Solar Energy Technology Holdings Limited and RBI Holdings Limited), a company listed on the Stock Exchange, for three years until 1 May 2008. 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 49, 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.

PROFILES OF DIRECTORS, SUPERVISORS AND SENIOR MANAGEMENT

Ms. Li Hongjian (李宏建), aged 59, 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).

Prof. Chen Yun Zhen (陳允震), aged 50, has been appointed as independent non-executive director on 31 December 2012. Prof. Chen is the supervisor of PhD candidates, professor and supervising doctor of Shandong University. Prof. Chen graduated at medical faculty of Shandong University in 1985 and has been working at the Orthopedic Department of Qilu Hospital since July 1985. Currently Prof. Chen is the deputy supervisor of Orthopedic Department, supervisor of Orthopedic Trauma Department and supervisor of Spinal Column and Spinal Cord Injury Research Centre of Qilu Hospital.

SUPERVISORS

Mr. Sun Song (孫松), aged 42, 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. Guan Yonghua (管永華), aged 50, 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.

Mr. Wang Jian (王健), aged 52, was appointed as a supervisor of the Company with effect from 30 November 2010. Mr. Wang graduated with a Master's degree in research from Shenyang Pharmacy University (瀋陽藥科大學). Mr. Wang worked as the head of research and development department and the general manger of Guangzhiu Bidi Pharmacy Co., Ltd (廣州彼迪藥業有限公司) prior to 1999 and has been individually researching in new medicine since 1999. Mr. Wang currently holds 16,640,136 Domestic Shares, representing approximately 3.74% of all Domestic Shares or approximately 2.73% of all Domestic Shares and H Shares.

Ms. Song Liang Wei (宋良偉), aged 32, was nominated by the staff congress of the Company and appointed as a supervisor of the Company with effect from 30 November 2010. Ms. Song is the manager of the New Medicine Research and Development Technical Centre of the Company. Ms. Song graduated with a diploma in professional pharmacy from Shandong University. Before joining the Company, Ms. Song worked at Linyi People Hospital.

SENIOR MANAGEMENT

Mr. Ji Honghai (季紅海), aged 38, 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. Before joining Shandong Luoxin Factory, he worked for Linyi Luozhuang from 1996 to 1997. Mr. Ji redesignated to another non-senior management position in January 2012.

PROFILES OF DIRECTORS, SUPERVISORS AND SENIOR MANAGEMENT

Mr. Zhao Xuekun (趙學昆), aged 77, 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. Zhao retired in January 2012.

Mr. Qian Chao Long (錢朝龍), aged 40, redesignated as the sales director of the Company in January 2012, responsible for the overall execution of the sales and marketing promotion of the Company. Before Mr. Qian joined the Company in 2007, he had been sales director of several medical companies for over 10 years and had over 16 years' experience in medicine sales field.

Ms. Li Ming Jie (李明傑), aged 44, redesignated as the Chief Engineer of the Company in January 2012 responsible for the production technique, craft management and research of the craft technology of the Company. Ms. Li graduated from Shenyang Pharmaceutical University and before joining the Company in 2002, she had been working with Harbin Pharmaceutical Group for 11 years. Ms. Li is the sister of Ms. Li Minghua.

Ms. Sun Ya Dong (孫亞東), aged 54, redesignated as the quality control authorised person of the Company in January 2012. Ms. Sun is responsible of the overall quality control and production workshop of the GMP certification project. Ms. Sun obtained Bachelor's degree of Chemical Pharmaceutical from Shenyang Pharmaceutical University, and is Senior Chemical Engineer and Registered Pharmacist awarded by Anhui Province Manpower Bureau. Before joining the Company in 2009, Ms. Sun had over 15 years of experience as Chief Engineer and quality control, and over 30 years' experience in pharmaceutical field.

Mr. Lau Hon Kee, Keith Vingo (劉漢基), FCPA, CPA (Aust.), aged 42, is the financial controller and company secretary of the Company. Mr. Lau is responsible for accounting, financial reporting and corporate governance 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 had been serving as an independent non-executive director of Strong Petrochemical Holdings Limited since November 2008 until December 2011, a company listed on the Stock Exchange. Mr. Lau 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 had over 10 years' experience in finance and accounting field, and held senior management position in several service and manufacturing companies.

MANAGEMENT DISCUSSION AND ANALYSIS

INTRODUCTION

As the PRC government proactively deepened medical reforms, continued to toughen regulations and standards and intensify investments in the pharmaceutical industry, and improved public health services in 2012, the investment into the development of medical and healthcare sector has been increasing. As a result, medical insurance coverage was expanded, rural health services were strengthened, and new rural cooperative medical services were enhanced. In addition to the above favourable factors, driven by the aging population, the accelerating urbanisation as well as the steady growth of the global pharmaceutical market, the development of the pharmaceutical industry in the PRC maintained the promising momentum in 2012.

As a leading modern pharmaceutical enterprise in the PRC, the Group has always been centering its strategies on science and technology innovation, research and development ("R&D") acceleration, distribution enhancement and production optimisation. Best endeavours were used to provide reliable, high-tech and high value-added pharmaceutical products. During the year under review, to fully leverage on the opportunities arising from the growth in the market, the Group satisfied market demands by investing additional resources in enhancing its production capabilities and technology application, and by accelerating the R&D of new products. Meanwhile, the Group has been keen on tapping into a broader market to increase its market share so as to boost its growth in both turnover and profits, thus building a solid foundation for sustainable future development of the Group.

BUSINESS REVIEW

For the year ended 31 December 2012, confronting the pressure in the market environment brought about by the commencement of public bidding of basic drugs, the launching of new Good Manufacturing Practices ("GMP") policy, drug-price cuts and restrictions on antibiotics, the Group has been implementing the development strategies as formulated earlier and sparing no effort in achieving the targets of the Twelfth Five-Year Plan, maintaining a balanced, healthy development in R&D, management, production, human resources and market network. 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. In view of the current achievements, the Group will strengthen its product R&D and expand its market network to further enhance its brand recognition and competitiveness with an aim to build up a world-class pharmaceutical brand.

RESEARCH AND DEVELOPMENT

1. *Building a platform for technology R&D*

   During the year under review, the Company obtained the approval from the National Development and Reform Commission to establish a state-province joint engineering laboratory. Prior to the year under review, the Group had established or been awarded the "Industrial Model Enterprise in the National Integrated Platform for New Pharmaceutical R&D 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), the "National Post-Doctoral Research Workstation" (國家博士後科研工作站) and "Key High-Tech Enterprise under the State Torch Program" (國家火炬計劃重點高新技術企業). On such basis, the Group obtained approvals to establish "Shandong Key Lyophilized Powder Injection Pharmaceutical Laboratory" (山東省凍乾粉針劑藥物重點實驗室), "Shandong Key Lyophilized Powder Injection Pharmaceutical Engineering Laboratory" (山東省凍乾粉針劑藥物工程實驗室), the position

of "Taishan Scholar – Pharmaceutical expert consultant" (泰山學者－藥學特聘專家) and "Enterprise Academician Workstation of Shandong Province" (山東省企業院士工作站), which enabled the Group to build a stronger platform for recruiting talents and improving technology and production technique, further strengthening the R&D capabilities and overall competitiveness of the Group.

2. *New products, patents and achievements*

During the year under review, the Group filed 48 invention patent applications in the PRC. As at 31 December 2012, the Group had 59 patents, of which 49 were invention patents registered in the PRC.

During the year under review, the Group obtained 12 manufacturing approvals for new products, bringing the total number of manufacturing approvals to 282 as at 31 December 2012.

During the year under review, the Group obtained 3 new drug certificates, bringing the total number of new drug certificates to 46 as at 31 December 2012.

During the year under review, the Company's product – "Aztreonam and Aztreonam for Injection" – was listed in the State Torch Program for 2012 (2012年度國家火炬計劃項目) by the Ministry of Science and Technology, bringing the total number of projects listed in the State Torch Program to 3 as at 31 December 2012.

PRODUCTION AND MANAGEMENT

1. The Group continued to implement effective strategies in seven integral systems, namely management, culture, corporate organisation, capital operation, science and technology innovation, human resources and marketing. These strategies have effectively contributed to the development of the Group and further enhanced its risk resistance capacities and overall competencies. The Company has been awarded the "Top 100 Pharmaceutical Companies in China" (中國制藥工業百強企業) consecutively since 2006. In 2012, the Company was once again awarded the "2012 Best Industrial Enterprise in terms of Pharmaceutical Product R&D and Production Line in China" (2012年中國醫藥研發產品線最佳工業企業) by the Ministry of Industry and Information Technology of the PRC. These recognitions demonstrated the growth in the overall corporate strength of the Group.

2. *Construction of Production Facilities*

(1) Pharmaceutical preparations: Shandong Yuxin Pharmacy Co., Ltd. was granted the Drug Manufacturing Certificate (藥品生產許可證), and the construction of its infusion workshop and ancillary facilities was completed. The current lyophilised powder injection workshop and solid preparation workshop built in compliance with the new national GMP standards have passed the certification of the new GMP.

(2) Pharmaceutical raw materials: the construction of pharmaceutical raw materials project of Shandong Hengxin Pharmacy Co., Ltd. is on fast track. Specifically, the synthetic raw materials workshop of the first phase of the project is in operation.

3. *External Investment*

During the year under review, teamed up with the People's Hospital of Fei County and Linyi People's Hospital, the Company established the Second People's Hospital of Fei County. With the investment of RMB40 million injected under the relevant cooperation agreement, the establishment and construction of the hospital is making smooth progress.

SALES AND MARKETING

The Group continued to integrate marketing resources and build up an outstanding sales team to increase market share and competitiveness of its products. At present, the Group has an extensive and seamless sales network throughout China under a well-established marketing management system, and accelerated the development of the rural market, and formed an OTC sales network, aiming to build the third terminal direct sales network.

FINANCIAL REVIEW

For the year ended 31 December 2012, the Group's audited turnover was approximately RMB2,228,257,000, representing an increase of approximately 36.97% from approximately RMB1,626,848,000 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 a sales network to increase the market share of its products, which boosted an increase in turnover.

For the year ended 31 December 2012, the audited cost of sales was approximately RMB725,977,000, representing an increase of approximately 16.30% from approximately RMB624,217,000 for the corresponding period of last year.

For the year ended 31 December 2012, the audited gross profit margin was 67.42%, representing an increase of approximately 5.79% from 61.63% 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, and improvement of production craft as a result of continuous investment on production facilities.

For the year ended 31 December 2012, the audited operating expenditure was approximately RMB1,020,181,000, representing an increase of approximately 92.15% from approximately RMB530,934,000 for the corresponding period of last year. The increase of operating expenditure was due to an increase in selling and distribution expenses in relation to new products launched during the year with different marketing strategies.

For the year ended 31 December 2012, the audited profit attributable to the shareholders was approximately RMB439,874,000 representing an increase of approximately 3.12% from approximately RMB426,556,000, for the corresponding period of last year. Weighted average earnings per share were RMB0.722 for the year ended 31 December 2012. The increase in the profit attributable to the shareholders was due to enhanced sales and products mix during the year.

MANAGEMENT DISCUSSION AND ANALYSIS

LIQUIDITY AND FINANCIAL RESOURCES

The Group's working capital is generally financed by its internally generated cash flow. As at 31 December 2012, the Group's cash and cash equivalents amounted to approximately RMB437,275,000 (as at 31 December 2011: RMB927,358,000). As at 31 December 2012, the Group did not have any borrowings (as at 31 December 2011: nil).

PLEDGED BANK DEPOSITS/CASH AND CASH EQUIVALENTS

As at 31 December 2012, the Group's bank deposits of approximately RMB101,940,000 were pledged as security for remittance under acceptance (as at 31 December 2011: bank deposits of approximately RMB34,481,000 were pledged as security for remittance under acceptance).

MAJOR ACQUISITION AND DISPOSAL

For the year ended 31 December 2012, the Group did not have any major acquisition or disposal.

SIGNIFICANT INVESTMENT

For the year ended 31 December 2012, the Group did not make any significant investment.

CONTINGENT LIABILITIES

As at 31 December 2012, 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 Company has established a remuneration committee to make recommendations on the overall strategy for remuneration policy.

MANAGEMENT DISCUSSION AND ANALYSIS

PROSPECTS

Looking ahead, the pharmaceutical industry will become one of the priorities of national policies, thus enjoying optimistic prospects. Being one of the supported key industries under the Twelfth Five-Year Plan, the pharmaceutical industry will enjoy more resources allocated by the Central Government to the pharmaceutical and medical equipment sectors, and a modern market system for the circulation of pharmaceutical products will be established during the period of the Twelfth Five-Year Plan so as to enhance industry concentration. The Group is confident in maintaining its sustainable and healthy development.

In addition, the "Guiding Opinions on Speeding up of the Restructuring of the Pharmaceutical Industry" (《關於加快醫藥行業結構調整的指導意見》) (the "Opinions") jointly published by the Ministry of Industry and Information Technology, the Ministry of Health and the State Food and Drug Administration of the PRC in November 2010 set out the goals of speeding up the restructuring of the pharmaceutical industry, cultivating independent innovation capability and enhancing production concentration. The Opinions are beneficial to the development of innovative enterprises as a whole as they provide more room for the growth of competitive enterprises.

In the future, the Group will continue to pursue the strategic direction of a "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 to enhance the standards in research and development as well as technologies, and to strengthen the capabilities of the internal research and development team. This will enable the Group to invent and develop more products of higher technology, better quality and higher added value. The Group also aims at reducing production cost and expanding production scale so as to achieve economies of scale, low production costs and a differentiated competitive edge. Upon the completion and commencement of production of its new plants of Yuxin and Hengxin, the Group will be able to increase its production capacity to satisfy the ever growing market demand for pharmaceutical products. The new plants will also help the introduction of new dosage forms and expand the R&D scope of new drugs more effectively, thus facilitating the Group's comprehensive business growth. The Group will also accelerate the establishment of its sales team and proactively broaden its sales network so as to enhance the market share of its products and continue to improve its core competitiveness.

Through the above strategies, the Group aspires to make "Luoxin" an internationally renowned brand in the pharmaceutical industry. With the rapid growth in productivity and the launch of more high value-added products, the Group is confident in maintaining a steady business growth and bringing satisfactory returns to its shareholders.

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 CORPORATE GOVERNANCE POLICY

The Board considers that good corporate governance of the Company is the key to safeguarding the interests of shareholders and enhancing the performance of the Company. The Board is committed to maintaining and ensuring 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.

The executive directors of the Board, according to the corporate governance policy, perform different duties in their specialist area, which are marketing, research and development, finance and accounting and general administration.

The Board has also established the Audit Committee, under its authorised terms of reference, to review the Company's existing internal control policies and procedures, operation, investor relationship and directors' duties and behaviour from time to time in order to maintain that the Board is managing the Company under the corporate governance policy.

In the opinion of the Directors, the Company complied with all the code provisions as set out in the Code on Corporate Governance Practices contained in the former Appendix 15 of the GEM Listing Rules from 1 January 2012 to 31 March 2012 and complied with all the code provisions as set out in Corporate Governance Code and Corporate Governance Report contained in the existing Appendix 15 of the GEM Listing Rules (the "New CG Code") from 1 April 2012 to 31 December 2012.

THE BOARD

The Board currently comprises of 5 executive Directors, namely, Mr. Liu Baoqi, Mr. Liu Zhenhai, Ms. Li Minghua, Mr. Han Fengsheng and Mr. Chen Yu with Mr. Liu Baoqi acting as chairman of the Board, currently 1 non-executive Director, namely, Mr. Yin Chuangui and 4 independent non-executive Directors, namely, Mr. Foo Tin Chung, Victor, Mr. Fu Hongzheng, Ms. Li Hongjian and Prof. Chen Yun Zhen. As the Company was established in the PRC, 4 supervisors namely, Mr. Sun Song, Mr. Guan Yonghua, Mr. Wang Jian and Ms. Song Liang Wei 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 service term of the Directors (including non-executive Directors) is for a period of 3 years running from 30 November 2010, the date on which the above Directors (other than Prof. Chen Yun Zhen) 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 at least 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 the 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 seek 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 Ordinance, 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 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 (or known as "Luoxin Pharmacy Group" today) during October 2007. But as they played a role in the Company's performance and transactions from 2008 to 2012, and will continue to play their role in subsequent events in 2013, the non-executive Director 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 judgement 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 the year 2012, 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 2012 are as follows:

	Dates of meeting			
Board Meetings	**13 March**	**8 May**	**7 August**	**6 November**
Executive Directors				
Mr. Liu Baoqi	✓	✓	✓	✓
Mr. Liu Zhenhai	✓	✓	✓	✓
Ms. Li Minghua	✓	✓	✓	✓
Mr. Han Fengsheng	✓	✓	✓	✓
Mr. Chen Yu	✓	✓	✓	✓
Non-executive Directors				
Mr. Yin Chuangui	✓	✓	✓	✓
Mr. Liu Yuxin (resigned on 31 December 2012)	✓	✓	✓	✓
Independent non-executive Directors				
Mr. Foo Tin Chung, Victor	✓	✓	✓	✓
Mr. Fu Hongzheng	✓	✓	✓	✓
Ms. Li Hongjian	✓	✓	✓	✓
Prof. Chen Yun Zhen (appointed on 31 December 2012)	X	X	X	X

CORPORATE GOVERNANCE REPORT

DIRECTORS' ATTENDANCE AT THE GENERAL MEETINGS

During the year under review, two general meetings were held and details of Directors' attendance are as follows:

Name of Directors	**15 May 2012 AGM**	**29 October 2012 EGM**
Executive Directors		
Mr. Liu Baoqi	✓	✓
Mr. Liu Zhenhai	✓	X
Ms. Li Minghua	✓	✓
Mr. Han Fengsheng	✓	✓
Mr. Chen Yu	✓	✓
Non-executive Directors		
Mr. Yin Chuangui	X	X
Mr. Liu Yuxin (resigned on 31 December 2012)	X	X
Independent non-executive Directors		
Mr. Foo Tin Chung, Victor	✓	X
Mr. Fu Hongzheng	✓	X
Ms. Li Hongjian	✓	X
Prof. Chen Yun Zhen (appointed on 31 December 2012)	X	X

CORPORATE GOVERNANCE REPORT

DIRECTORS' TRAINING

During the year under review, all the Directors have fulfilled the training requirement under paragraph A.6 of the New CG Code. The summary of the Directors who attended the types of training is as follows, and for the Director appointed during the year under review, he has also fulfilled the requirement on pro rata basis:

	Types of Training			
Name of Directors	**A**	**B**	**C**	**D**
Executive Directors				
Mr. Liu Baoqi	✓	✓	✓	✓
Mr. Liu Zhenhai	✓	X	✓	✓
Ms. Li Minghua	✓	✓	✓	✓
Mr. Han Fengsheng	✓	X	✓	✓
Mr. Chen Yu	✓	X	✓	✓
Non-executive Directors				
Mr. Yin Chuangui	✓	X	✓	✓
Mr. Liu Yuxin (resigned on 31 December 2012)	✓	X	✓	✓
Independent non-executive Directors				
Mr. Foo Tin Chung, Victor	X	X	✓	✓
Mr. Fu Hongzheng	X	X	✓	✓
Ms. Li Hongjian	X	X	✓	✓
Prof. Chen Yun Zhen (appointed on 31 December 2012)	X	X	✓	✓

A. Attending seminars or workshops on marketing issue of the industry, organised internally or by external providers;

B. Attending seminars or workshops on products research & development and technologies updates of the industry, organised internally or by external providers;

C. Attending seminar or workshops on the Listing Rules, corporate governance and compliance issues, organised internally or by external providers;

D. Attending seminar or workshops on directors' duties and undertakings, both organised internally or by external providers.

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 2012.

CORPORATE GOVERNANCE REPORT

CHAIRMAN AND CHIEF EXECUTIVE OFFICER

Under paragraph A.2.1 of the New CG 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 2012, 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.

COMMITTEES

As part of the corporate governance practices, the Board has established the following committees which are all chaired by and comprise of the 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 2012 included:

Mr. Foo Tin Chung, Victor *(Chairman)*
Mr. Fu Hongzheng
Ms. Li Hongjian
Prof. Chen Yun Zhen (appointed on 31 December 2012)

The Company has established the Audit Committee with written terms of reference in compliance with paragraph C.3 of the New CG Code. The terms of reference adopted on 20 November 2005 were amended and restated on 13 March 2012. The duties of the Audit Committee are to review and supervise the financial reporting process and the Company's internal control policies and procedures and the relationship with the Company's auditors. 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 Group for the year have been reviewed and discussed by the Audit Committee before any disclosure and release of information.

During the year ended 31 December 2012, the Audit Committee held four meetings and details of attendances of the meetings are shown below:

		Dates of meeting (2012)		
Audit Committee Meetings	**12 March**	**7 May**	**6 August**	**5 November**
Independent non-executive Directors				
Mr. Foo Tin Chung, Victor	✓	✓	✓	✓
Mr. Fu Hongzheng	✓	✓	✓	✓
Ms. Li Hongjian	✓	✓	✓	✓
Prof. Chen Yun Zhen (appointed on 31 December 2012)	X	X	X	X

CORPORATE GOVERNANCE REPORT

REMUNERATION COMMITTEE

The remuneration committee of the Company ("Remuneration Committee") was established in 20 November 2005 and its members during the year ended 31 December 2012 included:

Mr. Foo Tin Chung, Victor *(Chairman)*
Mr. Fu Hongzheng
Ms. Li Hongjian
Prof. Chen Yun Zhen (appointed on 31 December 2012)

The Company established the Remuneration Committee with written terms of reference in compliance with paragraph B.1 of the New CG Code. The terms of reference adopted on 20 November 2005 were amended and restated on 13 March 2012. The duties of the Remuneration Committee include evaluating the performance and making recommendations on the remuneration package of the Directors and senior management and evaluating 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. Amongst the members of the Remuneration Committee, Mr. Fu Hongzheng and Ms. Li Hongjian are both experienced medical professional in the PRC and Prof. Chen is a practising doctor and medical scholar.

During the year ended 31 December 2012, the Remuneration Committee held four meetings and details of the attendances of the meetings are shown below:

	Dates of meeting (2012)			
Remuneration Committee Meetings	**12 March**	**7 May**	**6 August**	**5 November**
Independent non-executive Directors				
Mr. Foo Tin Chung, Victor	✓	✓	✓	✓
Mr. Fu Hongzheng	✓	✓	✓	✓
Ms. Li Hongjian	✓	✓	✓	✓
Prof. Chen Yun Zhen (appointed on 31 December 2012)	X	X	X	X

NOMINATION COMMITTEE

The nomination committee of the Company ("Nomination Committee") was established on 13 March 2012 and its members during the year ended 31 December 2012 include:

Mr. Foo Tin Chung, Victor *(Chairman)*
Mr. Fu Hongzheng
Ms. Li Hongjian
Prof. Chen Yun Zhen (appointed on 31 December 2012)

The Company established the Nomination Committee with written terms of reference in compliance with paragraph A.5 of the New CG Code. The terms of reference were adopted on 13 March 2012. The duties of the Nomination Committee include reviewing the structure, size and composition of the Board, making recommendations on any proposed changes to the Board, identifying individuals suitably qualified to become Board members, assessing the independence of independent non-executive Directors, and making recommendations to the Board on the appointment or re-appointment of Directors and succession planning for Directors.

The appointments of the Nomination Committee members are based on their broad experience in the medicinal field and knowledge of directors' duties, in particular, the making of recommendation on the board composition with focus on different skills and knowledge of the Directors.

On 31 March 2012, the Nomination Committee issued nomination procedures in respect of shareholders' nomination of candidates for the Company's Directors.

During the year ended 31 December 2012, the Nomination Committee held three meetings and details of the attendances of the meetings are shown below:

	Dates of meeting (2012)		
Nomination Committee Meetings	**7 May**	**6 August**	**5 November**
Independent non-executive Directors			
Mr. Foo Tin Chung, Victor	✓	✓	✓
Mr. Fu Hongzheng	✓	✓	✓
Ms. Li Hongjian	✓	✓	✓
Prof. Chen Yun Zhen (appointed on 31 December 2012)	X	X	X

SHAREHOLDERS' RIGHTS

Extraordinary General Meeting

According to section 59 of the Articles of the Company, shareholders of the Company holding 10% or more of the total voting shares of the Company shall have the right to convene an extraordinary general meeting. Shareholders who would like to convene an extraordinary general meeting should send a written notice to the Board, which shall convene an extraordinary general meeting within two months after the receipt of the said written notice.

Shareholders of the Company who wish to make such proposal to convene an extraordinary general meeting should approach the Company Secretary for redirecting the proposal to the Board.

Making Proposals at Shareholders' Meetings

According to section 61 of the Articles of the Company, when the Company convenes an annual general meeting, shareholders holding 5% or more of the total voting shares of the Company shall have the right to propose new resolutions, and the Company shall include such proposed resolutions in the agenda for such annual general meeting if they are matters falling within the functions and powers of and to be dealt with by shareholders at general meetings.

Shareholders who would like to convene an extraordinary general meeting or to propose new resolutions in annual general meeting should approach the Company Secretary whom shall direct such request to the Board.

The contact of the Company Secretary:

The Company Secretary
Shandong Luoxin Pharmacy Stock Co. Ltd.
Room 110, Tower B, Southmark,
11 Yip Hing Street, Wong Chuk Hang,
Hong Kong

Email: keith.vingo.lau@luoxin.cn

Enquiries To The Board

Shareholders who would like to send enquiries to the Board could approach the Company Secretary in writing and the Board will reply the enquiries in a timely manner.

The contact of the Company Secretary:

The Company Secretary
Shandong Luoxin Pharmacy Stock Co. Ltd.
Room 110, Tower B, Southmark,
11 Yip Hing Street, Wong Chuk Hang,
Hong Kong

Email: keith.vingo.lau@luoxin.cn

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 interested parties;

* publication of announcements on the quarterly, interim and annual results on the Stock Exchange websites, and issuance 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 can be found on:

http://shandongluoxin.quamir.com

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 the 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 2012, the Board has reviewed the engagement of auditors and their remuneration. The auditor of the Company would receive approximately HK$600,000 for audit and related service and approximately HK$179,000 for other services.

The accounts for the year were audited by HLB Hodgson Impey Cheng Limited whose term of office will expire upon the forthcoming annual general meeting ("AGM") of the Company. The Audit Committee has recommended to the Board that HLB Hodgson Impey Cheng Limited be nominated for appointment as the auditors of the Company at the forthcoming AGM.

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 utilisation of the Company's resources and compliance with financial reporting and disclosure requirements. The Audit Committee will also advise 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 2012 (the "year").

THE STRATEGY TO GENERATE THE VALUE

The Company is committed to launching new medicines, with its strong product research and development support, at their highest yield of product lifecycle, which would maintain the growing return to the shareholders and advance medicine supplies to the community.

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 38 of this annual report.

The Directors recommend the payment of a final dividend of RMB0.3 per ordinary share, totaling RMB182,880,000. Such recommendation is subject to the approval of the shareholders of the Company at the forthcoming annual general meeting ("AGM") of the Company.

CLOSURE OF REGISTER OF MEMBERS

Annual General Meeting

The register of members of the Company will be closed from 10 May 2013 to 10 June 2013 (both days inclusive) in order to ascertain the shareholders who are eligible to attend and vote at the forthcoming AGM. All properly completed H Shares transfer forms accompanied by the relevant share certificates must be lodged with the Registrar 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 p.m. on 9 May 2013, for registration.

Entitlement to Final Dividend

The Board has recommended the payment of a final dividend of RMB0.3 per share in respect of the year ended 31 December 2012. Subject to the approval of shareholders at the forthcoming AGM, the dividend cum-date and ex-date will be 11 June 2013 and 13 June 2013 respectively. The register of members of the Company for entitlement of dividend will be closed from 17 June 2013 to 21 June 2013 (both days inclusive) in order to determine the shareholders who are eligible for the final dividend. All properly completed H shares transfer forms accompanied by the relevant share certificates must be lodged with the Registrar 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 p.m. on 14 June 2013, for registration.

REPORT OF THE DIRECTORS

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

Non-resident Corporate Shareholders

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 corporate shareholders whose names appear on the H Share register of members on 21 June 2013. The Company will distribute the final dividend to such non-resident corporate shareholders after withholding a 10% income tax. 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 17 June 2013 to 21 June 2013, 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 14 June 2013, for registration.

Non-resident Individual Shareholders

Pursuant to the regulation promulgated by the State General Administration of Taxation of the PRC (Guo Shui Han [2011] No.348), the Company is required to withhold and pay the non-resident individual income tax for the non-resident individual H shareholders and the non-resident individual H shareholders are entitled to certain tax preferential treatments according to the double tax treaties between those countries where the non-resident individual H shareholders are residents and China and the provisions in respect of double tax treaties between the mainland China and Hong Kong or Macau. The Company would withhold and pay the individual income tax at the tax rates of 10% on behalf of the non-resident individual H shareholders who are Hong Kong residents, Macau residents or residents of those countries having double tax treaties with China for personal income tax rates in respect of dividend of 10%. For non-resident individual H shareholders who are residents of those countries having agreements with China for personal income tax rates in respect of dividend of lower than 10%, the Company would make applications on their behalf to seek entitlement of the relevant agreed preferential treatments pursuant to the Notice of the State Administration of Taxation in relation to the Administrative Measures on Preferential Treatment Entitled by Non-residents under Tax Treaties (Tentative) (Guo Shui Fa [2009] No. 124) (《國家稅務總局關於印發〈非居民享受稅收協議待遇管理辦法（試行）〉的通知》（國稅發[2009]124號）). For non-resident individual H shareholders who are residents of those countries having double tax treaties with China for personal income tax rates in respect of dividend of higher than 10% but lower than 20%, the Company would withhold the individual income tax at the agreed-upon effective tax rate. For non-resident individual H shareholders who are residents of those countries without any double tax treaties with China or having double tax treaties with China for personal income tax in respect of dividend of 20% and other situations, the Company would withhold the individual income tax at a tax rate of 20%.

REPORT OF THE DIRECTORS

In order to determine the list of holders of H shares of the Company who are entitled to receive the final dividend, the H share register of members of the Company will be closed from 17 June 2013 to 21 June 2013, both days inclusive, during which period no transfer of the Company's H shares will be effected.

The Company will determine the country of domicile of the individual H shareholders based on the registered address as recorded in the register of members of the Company (the "Registered Address") on 21 June, 2013 and will withhold and pay the individual income tax based on the register of members of the Company as at 21 June 2013. If the country of domicile of the individual H shareholder is not the same as the Registered Address, the individual H shareholder shall notify the Company's H share registrar and provide relevant supporting documents Company's H share registrar in Hong Kong, Computershare Hong Kong Investors Services Limited, at 17M Floor, Hopewell Centre, 183 Queen's Road East, Wanchai, Hong Kong, no later than 4:30 p.m. on 14 June 2013, for registration. If any individual H shareholder does not provide the relevant supporting documents to the share registrar of the Company's H shares within the time period stated above, the Company will determine the country of domicile of such individual H shareholder(s) based on the recorded Registered Address on 21 June 2013.

The Company will strictly comply with the relevant PRC tax laws and regulations to withhold for payment such appropriate 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 21 June 2013.

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.

RESERVES

Movements in the reserves of the Company during the year are set out in Note 36 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 21 to the accounts.

SHARE CAPITAL

Details of the movements in share capital of the Company are set out in Note 35 to the accounts.

DISTRIBUTABLE RESERVES

According to the Company Law of the PRC, the distributable reserves of the Company as at 31 December 2012, amounted to RMB1,708,301,000 (2011: RMB1,390,394,000).

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 121 of this report.

COMPARISON BETWEEN BUSINESS OBJECTIVE AND ACTUAL BUSINESS PROGRESS

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

The promotional activities of 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 the relevant PRC authority.

PURCHASE, SALE OR REDEMPTION OF LISTED SECURITIES

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

SHARE OPTIONS

The Company has not adopted 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)

Non-executive directors

Liu, Yuxin (劉玉欣) (resigned on 31 December 2012)
Yin, Chuangui (尹傳貴)

REPORT OF THE DIRECTORS

Independent non-executive directors
Fu, Hongzheng (付宏征)
Foo, Victor Tin Chung (傅天忠)
Li Hongjian (李宏建)
Prof. Chen Yun Zhen (陳允震) (appointed on 31 December 2012)

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 Directors 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), Mr. Han Fengsheng (韓風生) and Mr. Chen Yu (陳雨), being executive Directors, retired and were re-elected on 24 November 2010 with a term of three years commencing from 30 November 2010.

Mr. Liu, Yuxin (劉玉欣) and Mr. Yin, Chuangui (尹傳貴), being non-executive Directors, retired and were re-elected on 24 November 2010 with a term of three years commencing from 30 November 2010. Mr. Liu, Yuxin (劉玉欣) resigned on 31 December 2012.

Mr. Fu, Hongzheng (付宏征), Mr. Foo, Victor Tin Chung (傅天忠) and Ms. Li Hongjian (李宏建), being independent non-executive Directors retired and were re-elected on 24 November 2010 with a term of three years commencing from 30 November 2010.

Prof. Chen Yun Zhen (陳允震) was appointed on 31 December 2012. In accordance with Article 96 of the Company, the term of service of Prof. Chen, who is appointed as independent non-executive Director on 31 December 2012 to fill in the casual vacancy of the Board, will expire at the next Annual General Meeting (the "AGM"). Accordingly, Prof. Chen will retire at the forthcoming AGM, and be eligible, as he indicated that he will offer himself, for re-election as independent non-executive Director.

Mr. Fu, Hongzheng (付宏征) and Mr. Foo, Victor Tin Chung (傅天忠) were appointed in June 2001 and April 2005 respectively and began to serve the Company since its listing on GEM in December 2005. And Ms. Li. HongjianIn (李宏建) was appointed on 30 November 2006. In accordance with the New CG Code paragraph A.4.3, shareholders vote on a separate resolution to retain an independent non-executive Director who has served on the board for more than nine years and the Company should include the reasons why the board considers the independent non-executive Director in the circular nominating him for election. Mr. Fu and Mr. Foo will be subject to a separate resolution with regard to their independence in the AGM to be held in 2014 and Ms. Li will be subject to this separate resolution in the AGM to be held in 2015.

REPORT OF THE DIRECTORS

DIRECTORS' SERVICE CONTRACTS

Except Prof. Chen Yun Zhen (陳允震), each of the executive Directors, non-executive Directors, independent non-executive Directors and supervisors of the Company has entered into a service contract with the Company commencing from 30 November 2011 for a term of three years.

Prof. Chen Yun Zhen's (陳允震) service contract was entered into on 31 December 2012. His term of service will expire at the forthcoming AGM. Accordingly, Prof. Chen will retire at the forthcoming AGM, and be eligible, as he indicated that he will offer himself, for re-election as independent non-executive Director.

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

DIRECTORS' AND SUPERVISORS' 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 2012, the interests and short positions of each of the 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 35 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 Shares"), as at 31 December 2012

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	325,639,949	73.17%	53.42%

Note 1:

These 325,639,949 Domestic Shares are registered in the name of Luoxin Pharmacy Group Co., Ltd. ("Luoxin Pharmacy Group", previously known as Linyi Luoxin Pharmacy Company Limited). Liu Baoqi (劉保起) ("Mr. Liu") is interested in 51.73% 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 325,639,949 Domestic Shares held by Luoxin Pharmacy Group. The total number of Domestic Shares deemed to be interested by Mr. Liu as at 31 December 2012 was 325,639,949 (representing 73.17% of total issued Domestic Shares and 53.42% of the Company's total issued share capital). On 30 June 2012, Luoxin Pharmacy Group held 320,639,949 Domestic Shares, representing 72.05% of the total issued Domestic Shares and 52.60% of the Company's total issued share capital. On 17 September 2012, Luoxin Pharmacy Group acquired 3,000,000 domestic shares from Mr. Li Xue Liang (李學良) and 2,000,000 domestic shares from Mr. Wang Jian (王健), a supervisor of the Company.

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 2012, 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 2012

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	325,639,949	73.17%	53.42%
Zuo Hongmei (左洪梅)	Family interest *(Note 2)*	325,639,949	73.17%	53.42%

Note 2:

These 325,639,949 Domestic Shares are registered in the name of Luoxin Pharmacy Group. Luoxin Pharmacy Group is owned as to approximately 51.73% 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 325,639,949 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 3 5,639,949 Domestic Shares that Mr. Liu is interested in.

CONTRACTS OF SIGNIFICANCE

During the year, the Company did not enter into any significant contract. However, the framework agreements of continuing connected transaction, entered into between the Company and (i) Luoxin Pharmacy Group, the controlling shareholder of the Company; (ii) Linyi People Hospital (iii) Shandong Luosheng Pharmacy Co., Ltd. ("Shandong Luosheng") and (iv) Shandong Mingxin Pharmacy Co., Ltd. ("Shandong Mingxin"), both being the fellow subsidiaries of the Company, in 2009 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.

REPORT OF THE DIRECTORS

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	6.88%
– five largest suppliers combined	25.29%
Sales	
– the largest customer	22.36%
– five largest customers combined	32.33%

During the year ended 31 December 2012, the sales of chemical medicines to Luoxin Pharmacy Group, Linyi People Hospital, Shandong Luosheng and Shandong Mingxin amounted to approximately RMB491,855,153, RMB Nil, RMB55,460,615 and RMB27,096,740 respectively. Luoxin Pharmacy Group is the largest customer of the Company for the year ended 31 December 2012.

Three of the five largest customers of the Company are Luoxin Pharmacy Group. Shandong Luosheng and Shandong Mingxin which are the related parties of the Company. For further details, please refer to note 39 to the accounts.

CONNECTED TRANSACTIONS AND CONTINUING CONNECTED TRANSACTIONS

During the year ended 31 December 2012, the Company had the following non-exempt continuing connected transactions, details of which are set out below:

	Annual Cap for the financial years ending 31 December		
Nature of transaction	**2010**	**2011**	**2012**
Sales of chemical medicines from the Company to Luoxin Pharmacy Group pursuant to a framework agreement dated 22 December 2009 and a supplemental framework agreement dated 4 April 2011	RMB200 million	RMB550 million	RMB825 million
Sales of chemical medicines by the Company to Linyi People Hospital pursuant to a framework agreement dated 22 December 2009	RMB25 million	RMB30 million	RMB39 million
Sales of chemical medicines by the Company to Shandong Luosheng pursuant to a framework agreement dated 22 December 2009 and a supplemental framework agreement dated 4 April 2011	RMB60 million	RMB120 million	RMB180 million
Sales of chemical medicines by the Company to Shandong Mingxin pursuant to a framework agreement dated 22 December 2009 and a supplemental framework agreement dated 4 April 2011	RMB55 million	RMB110 million	RMB165 million

Luoxin Pharmacy Group is the single largest and a substantial shareholder of the Company, holding approximately 53.42% of the issued share capital of the Company. Linyi People Hospital is one of the promoters of the Company. Shandong Luosheng and Shandong Mingxin are fellow subsidiaries of the Company of which Luoxin Pharmacy Group is holding more than 51% of both companies. 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, Shandong Luosheng and Shandong Mingxin pursuant to the respective framework agreements and supplemental framework agreements constitute continuing connected transactions of the Company, details of which are set out in the announcement issued by the Company on 5 January 2010 and 4 April 2011 and the circulars issued by the Company on 15 January 2010 and 15 April 2011.

REPORT OF THE DIRECTORS

During the year ended 31 December 2012, the sales of chemical medicines by the Company to Luoxin Pharmacy Group, Linyi People Hospital, Shandong Luosheng and Shandong Mingxin amounted to RMB491,855,153, RMB Nil, RMB55,460,615 and RMB27,096,740 (2011: RMB344,252,000, RMB Nil, RMB51,664,000 and RMB35,679,000) respectively which did not exceed the annual cap for the relevant transactions. Further details are set out in Note 39 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:–

1. in the ordinary and usual course of the business of the Company;

2. on terms of arm's length transactions to the Company; and

3. 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 INTERESTS

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

Luoxin Pharmacy Group

Luoxin Pharmacy Group which holds 53.42% of the Company's issued share capial, is the controlling shareholder of the Company. The chairman and executive director of the Company, Mr. Liu Baoqi, is also the chairman and executive director of Luoxin Pharmacy Group and a controlling shareholder thereof holding 51.73% of the registered capital of Luoxin Pharmacy Group.

The principal activities of Luoxin Pharmacy Group, apart from being a controlling Shareholder of the Company, are trading of medical equipment, Chinese medicines and health and beauty products, which are not directly or indirectly in competition with the Company's business. The Company is principally engaged in the manufacturing and trading of antibiotics and system specified medicines. Luoxin Pharmacy Group also engages in the trading of chemical medicines, but is restricted only to those products which are purchased from the Company under the continuing connected transactions as disclosed above. Save as trading of chemical medicines purchased from the Group, Luoxin Pharmacy Group does not sell any chemical medicine. The customers to whom Luoxin Pharmacy Group sells chemical medicines are those hospitals in Linyi City District which are at or below county level which the Group does not have direct access to.

REPORT OF THE DIRECTORS

Luoxin Pharmacy Group does not engage in the manufacturing of medicines whether by itself or through any subsidiary or associate company. Luoxin Pharmacy Group can only be regarded as participating in the manufacturing of medicines indirectly through the Group by reason of it being a controlling Shareholder of the Company.

The Company's targeted markets and customers are hospitals of all sizes and at all levels throughout the PRC. Luoxin Pharmacy Group's targeted markets and customers are small and medium sized hospitals at or below county level, mainly in Linyi City District.

Notwithstanding the non-competition undertakings entered into by Luoxin Pharmacy Group in 2002 (as supplemented by a memorandum in 2005), whereby it agreed not to engage in any business which would be in competition with that of the Company, the Company entered into certain continuing connected transactions with Luoxin Pharmacy Group pursuant to which the Company has been selling chemical medicines to Luoxin Pharmacy Group. It is a unique feature of the PRC medicine market that certain customer groups would only deal with certain medicine traders. Owing to this unique feature, certain hospitals at or below county level in Linyi City District would not purchase medicines directly from the Company. While Luoxin Pharmacy Group has business dealings with these hospitals, Luoxin Pharmacy Group becomes the bridge between the Group and those hospitals at or below county level in Linyi City District and sells the Company's chemical medicine products to them. Therefore, the Company entered into the said continuing connected transactions with Luoxin Pharmacy Group for the distribution of the Company's chemical medicines to these customers.

The Directors considered that not only were the continuing connected transactions not a breach of the non-competition undertaking on the part of Luoxin Pharmacy Group, but rather a perfect opportunity that promoted the cooperation between the Company and Luoxin Pharmacy Group in opening up the chemical medicine market and broaden the ultimate client base for both the Company and Luoxin Pharmacy Group with hospitals at or below county level in Linyi City District. Without this opportunity and cooperation, neither the Company nor Luoxin Pharmacy Group would be able to sell the chemical medicines to those hospitals. In reaching the above conclusion, the Directors have taken into account the following:

(i) there has been no sale of chemical medicines by Luoxin Pharmacy Group other than the chemical medicines purchased from the Company under the continuing connected transactions since 2005. As such, Luoxin Pharmacy Group has not resumed its chemical medicines business that is directly or indirectly in competition with the Company's business;

(ii) the continuing connected transactions bring mutual benefits to the Group and Luoxin Pharmacy Group. On one hand, the Group generates considerable revenue by distributing through Luoxin Pharmacy Group to particular groups of customers to which the Group would not be able to gain access without Luoxin Pharmacy Group. On the other hand, Luoxin Pharmacy Group generates revenue by selling the Group's products whilst pursuant to the undertakings, Luoxin Pharmacy Group is restricted from selling chemical medicine products produced by other manufacturers.

Revenue generated by the sale of products to Luoxin Pharmacy Group amounted to approximately 15%, 21% and 22% of the total revenue of the Company in each of the three years ended 31 December 2010, 2011 and 2012 respectively.

REPORT OF THE DIRECTORS

Despite the fact that the Group currently relies on Luoxin Pharmacy Group for a sizeable portion of its revenue, the Directors believe that there will be no difficulty for the Company to source other distributors and distribute its chemical medicine products to markets other than hospitals at or below county level in Linyi City District if Luoxin Pharmacy Group shall cease to distribute products of the Group. Having said that, the Company and Luoxin Pharmacy Group are in good business relationship and there is no indication that Luoxin Pharmacy Group will cease to cooperate with the Group.

In view of the above, the Directors consider there is no competing interest between the Group and Luoxin Pharmacy Group. None of the Directors, the substantial Shareholders of the Company or their respective associates (as defined in the Main Board 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 for the year were audited by HLB Hodgson Impey Cheng Limited whose term of office will expire upon the forthcoming AGM. A resolution for the appointment of HLB Hodgson Impey Cheng Limited as the auditors of the Company for the subsequent year is to be proposed at the forthcoming AGM.

On behalf of the Board
Liu Baoqi
Chairman

PRC, 19 March 2013

INDEPENDENT AUDITORS' REPORT

HLB 國衛會計師事務所有限公司
Hodgson Impey Cheng Limited

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 subsidiaries (collectively referred to as the "Group") set out on pages 39 to 120, which comprise the consolidated and company statements of financial position as at 31 December 2012, and the consolidated statement of comprehensive income, the consolidated statement of changes in equity and the consolidated statement of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information.

DIRECTORS' RESPONSIBILITY FOR THE CONSOLIDATED FINANCIAL STATEMENTS

The Directors of the Company are responsible for the preparation of consolidated financial statements that give a true and fair view 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, and for such internal control as the Directors determine is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

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 about whether the consolidated financial statements are free from material misstatement.

INDEPENDENT AUDITORS' REPORT

AUDITORS' RESPONSIBILITY (Continued)

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' judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditors consider internal control relevant to the entity's preparation of consolidated financial statements that give a true and fair view 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 and the Company as at 31 December 2012 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 Limited
Chartered Accountants
Certified Public Accountants

Hon Koon Fai, Alex
Practising Certificate Number: P05029

Hong Kong, 19 March 2013

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

For the year ended 31 December 2012

	Notes	2012 RMB'000	2011 RMB'000
Turnover	7	**2,228,257**	1,626,848
Cost of sales		**(725,977)**	(624,217)
Gross profit		**1,502,280**	1,002,631
Other revenue	7	**29,878**	9,023
Other income	9	**6,267**	15,614
Selling and distribution expenses		**(896,150)**	(403,313)
General and administrative expenses		**(124,031)**	(127,621)
Share of profit of an associate	17	**–**	5,873
Finance costs	8	**(90)**	(168)
Profit before taxation	9	**518,154**	502,039
Taxation	10	**(78,045)**	(75,355)
Profit for the year		**440,109**	426,684
Other comprehensive income for the year, net of tax			
– Share of other comprehensive income of an associate	17	**–**	1,620
Total comprehensive income for the year		**440,109**	428,304
Profit for the year attributable to:			
– Owners of the Company		**439,874**	426,556
– Non-controlling interests		**235**	128
		440,109	426,684
Total comprehensive income attributable to:			
– Owners of the Company		**439,874**	428,176
– Non-controlling interests		**235**	128
		440,109	428,304
Earnings per share attributable to owners of the Company (RMB)	15		
– Basic and diluted		**0.722**	0.700

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 2012

	Notes	2012 RMB'000	2011 RMB'000
Non-current assets			
Available-for-sale financial assets	18	**1,000**	1,000
Purchased technical know-how	19	**247**	677
Prepayments to acquire technical know-how	20	**16,245**	11,947
Property, plant and equipment	21	**273,695**	271,207
Construction-in-progress	22	**229,378**	116,414
Prepaid lease payments	23	**52,939**	19,687
Deferred tax assets	24	**1,972**	2,680
Goodwill	25	**165**	165
		575,641	423,777
Current assets			
Inventories	26	**188,344**	148,762
Trade and bills receivables	28	**312,882**	232,813
Other receivables, deposits and prepayments	29	**174,405**	104,573
Financial assets at fair value through profit and loss	30	**600,000**	100,000
Pledged bank deposits	31	**101,940**	34,481
Cash and bank balances	31	**335,335**	892,877
		1,712,906	1,513,506
Current liabilities			
Trade and bills payables	32	**217,493**	142,828
Other payables and accruals	33	**134,438**	171,209
Deposits received		**26,956**	26,787
Taxation payable		**50,341**	50,329
		429,228	391,153
Net current assets		**1,283,678**	1,122,353
Total assets less current liabilities		**1,859,319**	1,546,130

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

As at 31 December 2012

	Notes	2012 RMB'000	2011 RMB'000
Non-current liability			
Deferred income	34	**20,380**	20,380
Net assets		**1,838,939**	1,525,750
Capital and reserves			
Share capital	35	**60,960**	60,960
Other reserves		**67,781**	67,734
Retained earnings			
– Proposed final dividend		**182,880**	121,920
– Others		**1,525,421**	1,268,474
Equity attributable to owners of the Company		**1,837,042**	1,519,088
Non-controlling interests		**1,897**	6,662
Total equity		**1,838,939**	1,525,750

Approved by the Board of Directors on 19 March 2013 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 2012

	Notes	2012 RMB'000	2011 RMB'000
Non-current assets			
Interests in subsidiaries	16	**101,479**	118,979
Available-for-sale financial assets	18	**1,000**	1,000
Purchased technical know-how	19	**247**	677
Prepayments to acquire technical know-how	20	**16,245**	11,947
Property, plant and equipment	21	**273,116**	270,545
Construction-in-progress	22	**102,344**	14,061
Prepaid lease payments	23	**19,275**	19,687
Deferred tax assets	24	**1,972**	2,680
		515,678	439,576
Current assets			
Inventories	26	**185,910**	144,524
Amounts due from subsidiaries	27	**158,812**	184,375
Trade and bills receivables	28	**306,348**	224,495
Other receivables, deposits and prepayments	29	**135,898**	34,256
Financial assets at fair value through profit and loss	30	**600,000**	100,000
Pledged bank deposits	31	**95,940**	12,670
Cash and bank balances	31	**282,127**	770,483
		1,765,035	1,470,803
Current liabilities			
Trade and bills payables	32	**211,192**	118,270
Other payables and accruals	33	**133,533**	170,353
Deposits received		**26,593**	26,059
Taxation payable		**50,229**	50,329
		421,547	365,011
Net current assets		**1,343,488**	1,105,792
Total assets less current liabilities		**1,859,166**	1,545,368
Non-current liability			
Deferred income	34	**20,380**	20,380
Net assets		**1,838,786**	1,524,988

STATEMENT OF FINANCIAL POSITION

As at 31 December 2012

	Notes	2012 RMB'000	2011 RMB'000
Capital and reserves			
Share capital	35	**60,960**	60,960
Other reserves		**67,652**	67,652
Retained earnings			
– Proposed final dividend		**182,880**	121,920
– Others		**1,527,294**	1,274,456
Total equity		**1,838,786**	1,524,988

Approved by the Board of Directors on 19 March 2013 and signed on its behalf by:

Liu Baoqi
Director

Liu Zhenhai
Director

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

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

For the year ended 31 December 2012

	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	60,960	31,139	30,493	6,033	992,767	1,121,392	1,534	1,122,926
Profit for the year	–	–	–	–	426,556	426,556	128	426,684
Other comprehensive income for the year, net of tax:								
Share of other comprehensive income of an associate	–	–	–	–	1,620	1,620	–	1,620
Total comprehensive income for the year	–	–	–	–	428,176	428,176	128	428,304
Addition to non-controlling interests due to capital injection to a newly incorporated subsidiary	–	–	–	–	–	–	5,000	5,000
Transfer from retained earnings to statutory surplus reserve fund	–	–	69	–	(69)	–	–	–
Dividend paid	–	–	–	–	(30,480)	(30,480)	–	(30,480)
At 31 December 2011 and 1 January 2012	**60,960**	**31,139**	**30,562**	**6,033**	**1,390,394**	**1,519,088**	**6,662**	**1,525,750**
Profit for the year	**–**	**–**	**–**	**–**	**439,874**	**439,874**	**235**	**440,109**
Other comprehensive income for the year	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**
Total comprehensive income for the year	**—**	**—**	**—**	**—**	**439,874**	**439,874**	**235**	**440,109**
Capital refund to non-controlling interests due to deregistration of a subsidiary	**–**	**–**	**–**	**–**	**–**	**–**	**(5,000)**	**(5,000)**
Transfer from retained earnings to statutory surplus reserve fund	**–**	**–**	**47**	**–**	**(47)**	**–**	**–**	**–**
Dividend paid	**–**	**–**	**–**	**–**	**(121,920)**	**(121,920)**	**–**	**(121,920)**
At 31 December 2012	**60,960**	**31,139**	**30,609**	**6,033**	**1,708,301**	**1,837,042**	**1,897**	**1,838,939**
Representing:								
Proposed 2012 final dividends					**182,880**			
Others					**1,525,421**			
Retained earnings as at 31 December 2012					**1,708,301**			

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

CONSOLIDATED STATEMENT OF CASH FLOWS

For the year ended 31 December 2012

	Notes	2012 RMB'000	2011 RMB'000
Operating activities			
Profit before taxation		**518,154**	502,039
Adjustments for:			
Interest income		**(8,462)**	(7,142)
Interest expense		**90**	168
Interest income on financial assets at fair value through profit or loss		**(14,282)**	–
Share of profit of an associate	17	**–**	(5,873)
Reversal of obsolete inventories written down	26	**(3,960)**	(3,664)
Reversal of impairment loss recognised in respect of trade receivables	28	**(283)**	(4,301)
Reversal of impairment loss recognised in respect of other receivables	29	**(472)**	(650)
Depreciation of property, plant and equipment	21	**24,365**	22,265
Loss on disposal of property, plant and equipment		**1,139**	11
Write-down of obsolete inventories	26	**164**	4,104
Impairment loss recognised in respect of trade receivables	28	**1,068**	829
Impairment loss recognised in respect of other receivables	29	**1,392**	361
Amortisation of prepaid lease payments	23	**413**	413
Amortisation of purchased technical know-how	19	**430**	525
Operating cash flows before working capital changes		**519,756**	509,085
(Increase)/decrease in inventories		**(35,786)**	66,187
Increase in trade and bills receivables		**(80,854)**	(6,418)
Increase in other receivables, deposits and prepayments		**(104,416)**	(25,183)
Increase/(decrease) in trade and bills payables		**74,664**	(41,520)
Increase in deposits received		**169**	4,444
(Decrease)/increase in other payables and accruals		**(36,771)**	1,027
Cash generated from operations		**336,762**	507,622
Interest paid		**(90)**	(168)
PRC income tax paid		**(77,325)**	(66,164)
Net cash generated from operating activities		**259,347**	441,290

CONSOLIDATED STATEMENT OF CASH FLOWS

For the year ended 31 December 2012

	Notes	2012 RMB'000	2011 RMB'000
Investing activities			
Interest received		**8,462**	7,142
Acquisition of financial assets at fair value through profit or loss		**(1,050,000)**	(100,000)
Increase in prepayments to acquire technical know-how		**(4,298)**	(4,427)
Purchase of property, plant and equipment		**(19,379)**	(14,966)
Additions of construction-in-progress		**(121,577)**	(73,835)
Dividend received from associate		**–**	5,400
Proceeds from disposal of financial assets at FVTPL		**564,282**	–
Proceeds from disposal of interest in an associate		**–**	27,144
Net cash used in investing activities		**(622,510)**	(153,542)
Financing activities			
Dividend paid		**(121,920)**	(39,237)
Capital refund to non-controlling interests upon deregistration of a subsidiary		**(5,000)**	5,000
(Increase)/decrease in pledged bank deposits		**(67,459)**	57,356
Net cash (used in)/generated from financing activities		**(194,379)**	23,119
Net (decrease)/increase in cash and cash equivalents		**(557,542)**	310,867
Cash and cash equivalents at the beginning of the year		**892,877**	582,010
Cash and cash equivalents at the end of the year		**335,335**	892,877
Analysis of balances of cash and cash equivalents:			
Cash and bank balances		**335,335**	892,877

Note: Addition of prepaid lease payments of approximately RMB33,664,000 was paid in prior years. Therefore, no cash flows effect for the year ended 31 December 2012.

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2012

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 selling of pharmaceutical products. The principal activities of the subsidiaries are described in Note 16.

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 of Directors on 19 March 2013.

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

In the current year, the Group has adopted 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 2012.

HKFRS 1 (Amendments)	First-time Adoption of Hong Kong Financial Reporting Standards – Severe Hyperinflation and Removal of Fixed Dates for First-time Adopters
HKFRS 7 (Amendments)	Financial Instruments: Disclosures – Transfers of Financial Assets
HKAS 12 (Amendments)	Deferred Tax: Recovery of Underlying Assets

The Directors anticipate that the application of these new HKFRSs has no material impact on the results and the financial position of the Group.

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

The Group has not applied the following new and revised HKFRSs, that have been issued but are not yet effective, in these consolidated financial statements:

HKFRS 9	Financial Instruments[4]
HKFRS 10	Consolidated Financial Statements[2]
HKFRS 11	Joint Arrangements[2]
HKFRS 12	Disclosure of Interests in Other Entities[2]
HKFRS 13	Fair Value Measurement[2]
HKFRS 7 (Amendments)	Disclosures – Offsetting Financial Assets and Financial Liabilities[2]
HKFRS 9 and HKFRS 7 (Amendments)	Mandatory Effective Date of HKFRS 9 and Transition Disclosures[4]
HKFRS 10, HKFRS 11 and HKFRS 12 (Amendments)	Consolidated Financial Statements, Joint Arrangements Disclosure of Interests in Other Entities: Transition Guidance[2]
HKFRS 10, HKFRS 12 and HKAS 27 (Amendments)	Investment Entities[3]
HKAS 19 (as revised in 2011)	Employee Benefits[2]
HKAS 27 (as revised in 2011)	Separate Financial Statements[2]
HKAS 28 (as revised in 2011)	Investments in Associates and Joint Ventures[2]
HKAS 1 (Amendments)	Presentation of Items of Other Comprehensive Income[1]
HKAS 32 (Amendments)	Offsetting Financial Assets and Financial Liabilities[3]
HKFRSs (Amendments)	Annual Improvements to HKFRSs 2009-2011 Cycle[2]
HK(IFRIC)-Int 20	Stripping Costs in the Production Phase of a Surface Mine[2]

[1] effective for annual periods beginning on or after 1 July 2012

[2] effective for annual periods beginning on or after 1 January 2013

[3] effective for annual periods beginning on or after 1 January 2014

[4] effective for annual periods beginning on or after 1 January 2015

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

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

HKFRS 9 Financial Instruments

HKFRS 9 issued in 2009 introduced new requirements for the classification and measurement of financial assets. HKFRS 9 was amended in 2010 to include requirements for the classification and measurement of financial liabilities and for derecognition.

Key requirements of HKFRS 9 are described below:

- All recognised financial assets that are within the scope of HKAS 39 *Financial Instruments: Recognition and Measurement* to be subsequently measured at amortised cost or fair value. Specifically, debt investments that are held within a business model whose objective is to collect the contractual cash flows, and that have contractual cash flows that are solely payments of principal and interest on the principal outstanding are generally measured at amortised cost at the end of subsequent reporting periods. All other debt investments and equity investments are measured at their fair values at the end of subsequent accounting periods. In addition, under HKFRS 9, entities may make an irrevocable election to present subsequent changes in the fair value of an equity investment (that is not held for trading) in other comprehensive income, with only dividend income generally recognised in profit or loss.

- With regard to the measurement of financial liabilities designated as at fair value through profit or loss, HKFRS 9 requires that the amount of change in the fair value of the financial liability that is attributable to changes in the credit risk of that liability is presented in other comprehensive income, unless the recognition of the effects of changes in the liability's credit risk in other comprehensive income would create or enlarge an accounting mismatch in profit or loss. Changes in fair value of financial liabilities attributable to changes in the financial liabilities' credit risk are not subsequently reclassified to profit or loss. Previously, under HKAS 39, the entire amount of the change in the fair value of the financial liability designated as fair value through profit or loss was presented in profit or loss.

HKFRS 9 is effective for annual periods beginning on or after 1 January 2015, with earlier application permitted.

The Directors anticipate that the adoption of HKFRS 9 in the future may have a significant impact on the amounts reported in respect of the Group's financial assets and financial liabilities (e.g. the Group's available-for-sale investments may have to be measured at fair value at the end of subsequent reporting periods, with changes in the fair value being recognised in profit or loss). Regarding the Group's financial assets, it is not practicable to provide a reasonable estimate of that effect until a detailed review has been completed.

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

New and revised standards on consolidation, joint arrangements, associates and disclosures

In June 2011, a package of five standards on consolidation, joint arrangements, associates and disclosures was issued, including HKFRS 10, HKFRS 11, HKFRS 12, HKAS 27 (as revised in 2011) and HKAS 28 (as revised in 2011).

Key requirements of these five standards are described below.

HKFRS 10 replaces the parts of HKAS 27 *Consolidated and Separate Financial Statements* that deal with consolidated financial statements. HK (SIC)-Int 12 *Consolidation – Special Purpose Entities* will be withdrawn upon the effective date of HKFRS 10. Under HKFRS 10, there is only one basis for consolidation, that is, control. In addition, HKFRS 10 includes a new definition of control that contains three elements: (a) power over an investee, (b) exposure, or rights, to variable returns from its involvement with the investee, and (c) the ability to use its power over the investee to affect the amount of the investor's returns. Extensive guidance has been added in HKFRS 10 to deal with complex scenarios.

HKFRS 11 replaces HKAS 31 *Interests in Joint Ventures*. HKFRS 11 deals with how a joint arrangement of which two or more parties have joint control should be classified. HK (SIC) – Int 13 *Jointly Controlled Entities – Non-monetary Contributions by Venturers* will be withdrawn upon the effective date of HKFRS 11. Under HKFRS 11, joint arrangements are classified as joint operations or joint ventures, depending on the rights and obligations of the parties to the arrangements. In contrast, under HKAS 31, there are three types of joint arrangements: jointly controlled entities, jointly controlled assets and jointly controlled operations. In addition, joint ventures under HKFRS 11 are required to be accounted for using the equity method of accounting, whereas jointly controlled entities under HKAS 31 can be accounted for using the equity method of accounting or proportionate consolidation.

HKFRS 12 is a disclosure standard and is applicable to entities that have interests in subsidiaries, joint arrangements, associates and/or unconsolidated structured entities. In general, the disclosure requirements in HKFRS 12 are more extensive than those in the current standards.

In July 2012, the amendments to HKFRS 10, HKFRS 11 and HKFRS 12 were issued to clarify certain transitional guidance on the application of these five HKFRSs for the first time.

These five standards, together with the amendments relating to the transitional guidance, are effective for annual periods beginning on or after 1 January 2013 with earlier application permitted provided all of these standards are applied at the same time.

The Directors anticipate that the application of these five standards will have no impact to the Group's consolidated financial statements.

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

HKFRS 13 Fair Value Measurement

HKFRS 13 establishes a single source of guidance for fair value measurements and disclosures about fair value measurements. The standard defines fair value, establishes a framework for measuring fair value, and requires disclosures about fair value measurements. The scope of HKFRS 13 is broad; it applies to both financial instrument items and non-financial instrument items for which other HKFRSs require or permit fair value measurements and disclosures about fair value measurements, except in specified circumstances. In general, the disclosure requirements in HKFRS 13 are more extensive than those in the current standards. For example, quantitative and qualitative disclosures based on the three-level fair value hierarchy currently required for financial instruments only under HKFRS 7 *Financial Instruments: Disclosures* will be extended by HKFRS 13 to cover all assets and liabilities within its scope.

HKFRS 13 is effective for annual periods beginning on or after 1 January 2013, with earlier application permitted.

The Directors anticipate that the application of the new standard may affect certain amounts reported in the consolidated financial statements and result in more extensive disclosures in the consolidated financial statements.

HKFRS 7 and HKAS 32 (Amendments) Offsetting Financial Assets and Financial Liabilities and the related disclosures

The amendments to HKAS 32 clarify existing application issues relating to the offset of financial assets and financial liabilities requirements. Specifically, the amendments clarify the meaning of "currently has a legally enforceable right of set-off" and "simultaneous realisation and settlement".

The amendments to HKFRS 7 require entities to disclose information about rights of offset and related arrangements (such as collateral posting requirements) for financial instruments under an enforceable master netting agreement or similar arrangement.

The amendments to HKFRS 7 are effective for annual periods beginning on or after 1 January 2013 and interim periods within those annual periods. The disclosures should be provided retrospectively for all comparative periods. However, the amendments to HKAS 32 are not effective until annual periods beginning on or after 1 January 2014, with retrospective application required.

The Directors anticipate that the application of these amendments to HKAS 32 and HKFRS 7 may result in more disclosures being made with regard to offsetting financial assets and financial liabilities in the future.

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

HKAS 1 (Amendments) Presentation of Items of Other Comprehensive Income

The amendments to HKAS 1 introduce new terminology for the statement of comprehensive income and income statement. Under the amendments to HKAS 1, a statement of comprehensive income is renamed as a statement of profit or loss and other comprehensive income and an income statement is renamed as a statement of profit or loss. The amendments to HKAS 1 retain the option to present profit or loss and other comprehensive income in either a single statement or in two separate but consecutive statements. However, the amendments to HKAS 1 require items of other comprehensive income to be grouped into two categories in the other comprehensive income section: (a) items that will not be reclassified subsequently to profit or loss and (b) items that may be reclassified subsequently to profit or loss when specific conditions are met. Income tax on items of other comprehensive income is required to be allocated on the same basis. The amendments do not change the option to present items of other comprehensive income either before tax or net of tax.

The amendments to HKAS 1 are effective for annual periods beginning on or after 1 July 2012. The presentation of items of other comprehensive income will be modified accordingly when the amendments are applied in the future accounting periods.

Annual Improvements to HKFRSs 2009 – 2011 Cycle issued in June 2012

The Annual Improvements to HKFRSs 2009 – 2011 Cycle include a number of amendments to various HKFRSs. The amendments are effective for annual periods beginning on or after 1 January 2013. Amendments to HKFRSs include:

- amendments to HKAS 1 Presentation of Financial Statements;
- amendments to HKAS 16 Property, Plant and Equipment; and
- amendments to HKAS 32 Financial Instruments: Presentation.

HKAS 1 (Amendments)

HKAS 1 requires an entity that changes accounting policies retrospectively, or makes a retrospective restatement or reclassification to present a statement of financial position as at the beginning of the preceding period (third statement of financial position). The amendments to HKAS 1 clarify that an entity is required to present a third statement of financial position only when the retrospective application, restatement or reclassification has a material effect on the information in the third statement of financial position and that related notes are not required to accompany the third statement of financial position.

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

Annual Improvements to HKFRSs 2009 – 2011 Cycle issued in June 2012 (continued)

HKAS 16 (Amendments)

The amendments to HKAS 16 clarify that spare parts, stand-by equipment and servicing equipment should be classified as property, plant and equipment when they meet the definition of property, plant and equipment in HKAS 16 and as inventory otherwise. The Directors do not anticipate that the amendments to HKAS 16 will have a significant effect on the Group's consolidated financial statements.

HKAS 32 (Amendments)

The amendments to HKAS 32 clarify that income tax on distributions to holders of an equity instrument and transaction costs of an equity transaction should be accounted for in accordance with HKAS 12 *Income Taxes*. The Directors anticipate that the amendments to HKAS 32 will have no effect on the Group's consolidated financial statements.

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.

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. Historical cost is generally based on the fair value of the consideration given in exchange for assets.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Basis of consolidation

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

Income and expenses of subsidiaries acquired or disposed of during the year are included in the consolidated statement of comprehensive income from the effective date of acquisition and up to the effective date of disposal, as appropriate. Total comprehensive income of subsidiaries is attributed to the owners of the Company and to the non-controlling interests even if this results in the non-controlling interests having a deficit balance.

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

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

Changes in the Group's ownership interests in existing subsidiaries

Changes in the Group's ownership interests in subsidiaries that do not result in the Group losing control over the subsidiaries are accounted for as equity transactions. The carrying amounts of the Group's interests and the non-controlling interests are adjusted to reflect the changes in their relative interests in the subsidiaries. Any difference between the amount by which the non-controlling interests are adjusted and the fair value of the consideration paid or received is recognised directly in equity and attributed to owners of the Company.

When the Group loses control of a subsidiary, it (i) derecognises the assets (including any goodwill) and liabilities of the subsidiary at their carrying amounts at the date when control is lost, (ii) derecognises the carrying amount of any non-controlling interest in the former subsidiary at the date when control is lost (including any components of other comprehensive income attributable to them), and (iii) recognises the aggregate of the fair value of the consideration received and the fair value of any retained interest, with any resulting difference being recognised as a gain or loss in profit or loss attributable to the Group. When assets of the subsidiary are carried at revalued amounts or fair values and the related cumulative gain or loss has been recognised in other comprehensive income and accumulated in equity, the amounts previously recognised in other comprehensive income and accumulated in equity are accounted for as if the Group had directly disposed of the related assets (i.e. reclassified to profit or loss or transferred directly to retained earnings as specified by applicable HKFRSs). The fair value of any investment retained in the former subsidiary at the date when control is lost is regarded as the fair value on initial recognition for subsequent accounting under HKAS 39 *Financial Instruments: Recognition and Measurement* or, when applicable, the cost on initial recognition of an investment in an associate or a jointly controlled entity.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Business combinations

Acquisitions of businesses are accounted for using the acquisition method. The consideration transferred in a business combination is measured at fair value, which is calculated as the sum of the acquisition-date fair values of the assets transferred by the Group, liabilities incurred by the Group to the former owners of the acquiree and the equity interests issued by the Group in exchange for control of the acquiree. Acquisition-related costs are generally recognised in profit or loss as incurred.

At the acquisition date, the identifiable assets acquired and the liabilities assumed are recognised at their fair value, except that:

- deferred tax assets or liabilities, and assets or liabilities related to employee benefit arrangements are recognised and measured in accordance with HKAS 12 *Income Taxes* and HKAS 19 *Employee Benefits* respectively;

- liabilities or equity instruments related to share-based payment arrangements of the acquiree or share-based payment arrangements of the Group entered into to replace share-based payment arrangements of the acquiree are measured in accordance with HKFRS 2 *Share-based Payment* at the acquisition date; and

- 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* are measured in accordance with that standard.

Goodwill is measured as the excess of the sum of the consideration transferred, the amount of any non-controlling interests in the acquiree, and the fair value of the acquirer's previously held equity interest in the acquiree (if any) over the net of the acquisition-date amounts of the identifiable assets acquired and the liabilities assumed. If, after reassessment, the net of the acquisition-date amounts of the identifiable assets acquired and liabilities assumed exceeds the sum of the consideration transferred, the amount of any non-controlling interests in the acquiree and the fair value of the acquirer's previously held interest in the acquiree (if any), the excess is recognised immediately in profit or loss as a bargain purchase gain.

Non-controlling interests that are present ownership interests and entitle their holders to a proportionate share of the entity's net assets in the event of liquidation may be initially measured either at fair value or at the non-controlling interests' proportionate share of the recognised amounts of the acquiree's identifiable net assets. The choice of measurement basis is made on a transaction-by-transaction basis. Other types of non-controlling interests are measured at their fair value or, when applicable, on the basis specified in another HKFRS.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Business combinations (Continued)

Where the consideration transferred by the Group in a business combination includes assets or liabilities resulting from a contingent consideration arrangement, the contingent consideration is measured at its acquisition-date fair value and included as part of the consideration transferred in a business combination. Changes in the fair value of the contingent consideration that qualify as measurement period adjustments are adjusted retrospectively, with the corresponding adjustments against goodwill. Measurement period adjustments are adjustments that arise from additional information obtained during the "measurement period" (which cannot exceed one year from the acquisition date) about facts and circumstances that existed at the acquisition date.

The subsequent accounting for changes in the fair value of the contingent consideration that do not qualify as measurement period adjustments depends on how the contingent consideration is classified. Contingent consideration that is classified as equity is not remeasured at subsequent reporting dates and its subsequent settlement is accounted for within equity. Contingent consideration that is classified as an asset or a liability is remeasured at subsequent reporting dates in accordance with HKAS 39, or HKAS 37 *Provisions, Contingent Liabilities and Contingent Assets*, as appropriate, with the corresponding gain or loss being recognised in profit or loss.

When a business combination is achieved in stages, the Group's previously held equity interest in the acquiree is remeasured to fair value at the acquisition date (i.e. the date when the Group obtains control), and the resulting gain or loss, if any, is recognised in profit or loss. Amounts arising from interests in the acquiree prior to the acquisition date that have previously been recognised in other comprehensive income are reclassified to profit or loss where such treatment would be appropriate if that interest were disposed of.

If the initial accounting for a business combination is incomplete by the end of the reporting period in which the combination occurs, the Group reports provisional amounts for the items for which the accounting is incomplete. Those provisional amounts are adjusted during the measurement period (see above), or additional assets or liabilities are recognised, to reflect new information obtained about facts and circumstances that existed at the acquisition date that, if known, would have affected the amounts recognised at that date.

Goodwill

Goodwill arising on an acquisition of a business is carried at cost as established at the date of acquisition of the business less accumulated impairment losses, if any.

For the purposes of impairment testing, goodwill is allocated to each of the Group's cash-generating units (or groups of cash-generating units) that is expected to benefit from the synergies of the combination.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Goodwill (Continued)

A cash-generating unit to which goodwill has been allocated is tested for impairment annually, or more frequently when there is indication that the unit may be impaired. If the recoverable amount of the cash-generating unit is less than its carrying amount, the impairment loss is allocated first to reduce the carrying amount of any goodwill allocated to the unit, and then to the other assets of the unit on a pro rata basis based on the carrying amount of each asset in the unit. Any impairment loss for goodwill is recognised directly in profit or loss. An impairment loss recognised for goodwill is not reversed in subsequent periods.

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

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, except when the investment is classified as held for sale, in which case it is accounted for in accordance with HKFRS 5 *Non-current Assets Held for Sale and Discontinued Operations*. Under the equity method, investment in an associate is initially recognised in the consolidated statement of financial position at cost and adjusted thereafter to recognise the Group's share of the profit or loss and other comprehensive income of the associate. 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 recognised 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 an associate recognised at the date of acquisition is recognised as goodwill, which is included within the carrying amount of the investment.

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.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Investment in an associate (continued)

The requirements of HKAS 39 are applied to determine whether it is necessary to recognise any impairment loss with respect to the Group's investment in an associate. When necessary, the entire carrying amount of the investment (including goodwill) is tested for impairment in accordance with HKAS 36 *Impairment of Assets* as a single asset by comparing its recoverable amount (higher of value in use and fair value less costs to sell) with its carrying amount. Any impairment loss recognised forms part of the carrying amount of the investment. Any reversal of that impairment loss is recognised in accordance with HKAS 36 to the extent that the recoverable amount of the investment subsequently increases.

Upon disposal of an associate that results in the Group losing significant influence over that associate, any retained investment is measured at fair value at that date and the fair value is regarded as its fair value on initial recognition as a financial asset in accordance with HKAS 39. The difference between the previous carrying amount of the associate attributable to the retained interest and its fair value is included in the determination of the gain or loss on disposal of the associate. In addition, the Group accounts for all amounts previously recognised in other comprehensive income in relation to that associate on the same basis as would be required if that associate had directly disposed of the related assets or liabilities. Therefore, if a gain or loss previously recognised in other comprehensive income by that associate would be reclassified to profit or loss on the disposal of the related assets or liabilities, the Group reclassifies the gain or loss from equity to profit or loss (as a reclassification adjustment) when it loses significant influence over that associate.

When a group entity transacts with its associate, profits and losses resulting from the transactions with the associate are recognised in the Group's consolidated financial statements only to the extent of interests in the associate that are not related to the Group.

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.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Property, plant and equipment (Continued)

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.

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

When a lease includes both land and building elements, the Group assesses the classification of each element as a finance or an operating lease separately based on the assessment as to whether substantially all the risks and rewards incidental to ownership of each element have been transferred to the Group, unless it is clear that both elements are operating leases in which case the entire lease is classified as an operating lease. Specifically, the minimum lease payments (including any lump-sum upfront payments) are allocated between the land and the building elements in proportion to the relative fair values of the leasehold interests in the land element and building element of the lease at the inception of the lease.

To the extent the allocation of the lease payments can be made reliably, interest in leasehold land that is accounted for as an operating lease is presented as "prepaid lease payments" in the consolidated statement of financial position and is amortised over the lease term on a straight-line basis. When the lease payments cannot be allocated reliably between the land and building elements, the entire lease is generally classified as a finance lease and accounted for as property, plant and equipment.

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. The estimated useful life and amortisation method are reviewed at the end of each reporting period, with the effect of any changes in estimate being accounted for on a prospective basis.

Impairment of tangible and intangible assets other than goodwill

At the end of each reporting period, the Group reviews the carrying amounts of its tangible and intangible assets with finite useful lives 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. Where it is not possible to estimate the recoverable amount of an individual asset, the Group estimates the recoverable amount of the cash-generating unit to which the asset belongs. Where a reasonable and consistent basis of allocation can be identified, corporate assets are also allocated to individual cash-generating units, or otherwise they are allocated to the smallest group of cash-generating units for which a reasonable and consistent allocation basis can be identified.

Intangible assets with indefinite useful lives and intangible assets not yet available for use are tested for impairment at least annually, and whenever there is an indication that the asset may be impaired.

Recoverable amount is the higher of fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset for which the estimates of future cash flows have not been adjusted.

If the recoverable amount of an asset (or a cash-generating unit) is estimated to be less than its carrying amount, the carrying amount of the asset (or the cash-generating unit) is reduced to its recoverable amount. An impairment loss is recognised immediately in profit or loss.

Where an impairment loss subsequently reverses, the carrying amount of the asset (or a cash-generating unit) 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 (or a cash-generating unit) in prior years. A reversal of an impairment loss is recognised immediately in profit or loss.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

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.

Financial assets

The Group's financial assets are classified into loans and receivables, financial assets at fair value though profit or loss and available-for-sale financial assets ("AFS financial assets"). The classification depends on the nature and purpose of the financial assets and is determined at the time of initial recognition. 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 and 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 those financial assets classified as at fair value through profit or loss.

Financial assets at fair value though profit or loss

Financial assets are classified as at fair value though profit or loss when the financial asset is either held for trading or it is designated as at fair value though profit or loss.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Financial instruments (Continued)

Financial assets (Continued)

Financial assets at fair value though profit or loss (Continued)

A financial asset is classified as held for trading if:

- it has been acquired principally for the purpose of selling 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 asset other than a financial asset held for trading may be designated as at fair value though 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 asset 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 Financial Instruments: Recognition and Measurement permits the entire combined contract (asset or liability) to be designated as at fair value though profit or loss.

Financial assets at fair value though 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 incorporates any dividend or interest earned on the financial asset and is included in the "other gains and losses" line item. Fair value is determined in the manner described in Note 5.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2012

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Financial instruments (Continued)

Financial assets (Continued)

AFS financial assets

AFS financial assets are non-derivatives that are either designated as available-for-sale or are not classified as loans and receivables, held-to-maturity investments or financial assets at fair value through profit or loss.

Equity and debt securities held by the Group that are classified as AFS financial assets and are traded in an active market are measured at fair value at the end of each reporting period. Changes in the carrying amount of AFS monetary financial assets relating to interest income calculated using the effective interest method and dividends on AFS equity investments are recognised in profit or loss. Other changes in the carrying amount of AFS financial assets are recognised in other comprehensive income and accumulated under the heading of investments revaluation reserve. Where the investment is disposed of or is determined to be impaired, the cumulative gain or loss previously accumulated in the investments revaluation reserve is reclassified to profit or loss.

Dividends on AFS equity investments are recognised in profit or loss when the Group's right to receive the dividends is established.

AFS equity investments that do not have a quoted market price in the active market and whose fair value cannot be reliably measured and derivatives that are linked to and must be settled by delivery of such unquoted equity investments are measured at cost less any identified impairment losses at the end of each reporting period.

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.

Interest income is recognised by applying the effective interest rate, except for short-term receivables when the recognition of interest would be immaterial.

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 each reporting period. Financial assets are considered to be impaired when 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 AFS equity investments, a significant or prolonged decline in the fair value of the security below its cost is considered to be objective evidence of impairment.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Financial instruments (Continued)

Financial assets (Continued)

Impairment of financial assets (Continued)

For all other financial assets, objective evidence of impairment could include:

- significant financial difficulty of the issuer or counterparty; or
- breach of contract, such as default or delinquency in interest or principal payments; or
- it becoming probable that the borrower will enter bankruptcy or financial re-organisation; or
- the disappearance of an active market for that financial asset because of financial difficulties.

For certain categories of financial assets, such as trade receivables, assets that are assessed not to be impaired individually are, in addition, 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.

For financial assets carried at amortised cost, the amount of the impairment loss recognised 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.

For financial assets carried at cost, the amount of the impairment loss is measured as the difference between the asset's carrying amount and the present value of the estimated future cash flows discounted at the current market rate of return for a similar financial asset. Such impairment loss will not be reversed in subsequent periods.

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.

When an AFS financial asset is considered to be impaired, cumulative gains or losses previously recognised in other comprehensive income are reclassified to profit or loss in the period.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Financial instruments (Continued)

Financial assets (Continued)

Impairment of financial assets (Continued)

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.

In respect of AFS equity investments, impairment losses previously recognised in profit or loss are not reversed through profit or loss. Any increase in fair value subsequent to an impairment loss is recognised in other comprehensive income and accumulated under the heading of investments revaluation reserve. In respect of AFS debt securities, impairment losses are subsequently reversed through profit or loss if an increase in the fair value of the investment can be objectively related to an event occurring after the recognition of the impairment loss.

Financial liabilities and equity instruments

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.

The Group's financial liabilities are generally classified into financial liabilities at fair value through profit or loss and other financial liabilities.

Equity instruments

An equity instrument is any contract that evidences a residual interest in the assets of an entity after deducting all of its liabilities. Equity instruments issued by the Group are recognised at the proceeds received, net of direct issue costs.

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.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Financial instruments (Continued)

Financial liabilities and equity instruments (Continued)

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

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 *Financial Instruments: Recognition and Measurement* permits the entire combined contract (asset or liability) to be designated as at fair value through profit or loss.

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 incorporates any interest paid on the financial liability.

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.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Financial instruments (Continued)

Financial liabilities and equity instruments (Continued)

Effective interest method

The effective interest method is a method of calculating the amortised cost of a financial liability and of allocating interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments (including all fees and 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.

Derecognition

The Group derecognises a financial asset only when the contractual rights to the cash flows from the asset expire, or when it transfers the financial asset and 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 continues to recognise the asset to the extent of its continuing involvement and recognises an associated liability. 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 in its entirety, 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.

On derecognition of a financial asset other than in its entirety, the Group allocates the previous carrying amount of the financial asset between the part it continues to recognise, and the part it no longer recognises on the basis of the relative fair values of those parts on the date of the transfer. The difference between the carrying amount allocated to the part that is no longer recognised and the sum of the consideration received for the part no longer recognised and any cumulative gain or loss allocated to it that had been recognised in other comprehensive income is recognised in profit or loss. A cumulative gain or loss that had been recognised in other comprehensive income is allocated between the part that continues to be recognised and the part that is no longer recognised on the basis of the relative fair values of those parts.

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.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

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.

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 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. When 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 of the time value of money is material).

When some or all of the economic benefits required to settle a provision are expected to be recovered from a third party, a receivable is recognised as an asset if it is virtually certain that reimbursement will be received and the amount of the receivable can be measured reliably.

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 before taxation" 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.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Income tax (Continued)

Current and deferred tax for the year is recognised in profit or loss, except when they relate to items that are recognised in other comprehensive income or directly in equity, in which case, the current and deferred tax are also recognised in other comprehensive income or directly in equity respectively. Where current tax or deferred tax arises from the initial accounting for a business combination, the tax effect is included in the accounting for the business combination.

Revenue recognition

Revenue is measured at the fair value of the consideration received or receivable. Revenue is reduced for estimated customer returns, rebates and other similar allowances.

Revenue from the sale of goods is recognised when the goods are delivered and titles have passed, at which time 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 is recognised when it is probable that the economic benefits will flow to the Group and the amount of income can be measured reliably. Interest income 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.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2012

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

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 end of the reporting period. 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.

Borrowing costs

Borrowings costs directly attributable to the acquisition, construction or production of qualifying assets, which are assets that necessarily take a substantial period of time to get ready for their intended use or sale, are added to the cost of those assets, until such time as the assets are substantially ready for their intended use or sale.

Investment income earned on the temporary investment of specific borrowings pending their expenditure on qualifying assets is deducted from the borrowing costs eligible for capitalisation.

All other borrowing costs are recognised in profit or loss in the period in which they are incurred.

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.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Foreign and presentation currency (Continued)

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.

Related party transactions

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

(a) the party or a close member of that person's family is related to the Group if that person:

   (i) has control or joint control over the Group;

   (ii) has significant influence over the Group; or

   (iii) is a member of the key management personnel of the Group or of a parent of the reporting entity.

(b) an entity is related to the Group if any of the following conditions applies:

   (i) the entity and the Group are members of the same group (which means that each parent, subsidiary and fellow subsidiary is related to the others);

   (ii) one entity is an associate or joint venture of the other entity (or an associate or joint venture of a member of a group of which the other entity is a member);

   (iii) both entities are joint ventures of the same third party;

   (iv) one entity is a joint venture of a third entity and the other entity is an associate of the third entity;

   (v) the entity is a post-employment benefit plan for the benefit of employees of either the Group or an entity related to the Group. If the Group is itself such a plan, the sponsoring employers are also related to the Group;

   (vi) the entity is controlled or jointly controlled by a person identified in (a)); and

   (vii) a person identified in (a)(i) has significant influence over the entity or is a member of the key management personnel of the entity (or of a parent of the entity).

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Related party transactions (Continued)

Close family members of an individual are those family members who may be expected to influence, or be inflecting by, that person in their dealings with the entity.

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

In the application of the Group's accounting policies, which are described in Note 3, management is required to make judgements, estimates and assumptions about the carrying amounts of assets and liabilities that are not readily apparent from other sources. The estimates and underlying assumptions are based on historical experience and other factors that are considered to be relevant. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate 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.

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.

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.

4. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS (Continued)

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.

5. FINANCIAL INSTRUMENTS AND CAPITAL RISK MANAGEMENT

(a) Categories of financial instruments

	2012	2011
	RMB'000	RMB'000
The Group		
Financial assets		
Available-for-sale investments	**1,000**	1,000
Loan and receivables (including cash and cash equivalents)	**835,991**	1,174,415
Financial assets at fair value through profit or loss	**600,000**	100,000
Financial liabilities		
Amortised cost	**319,703**	294,279

5. FINANCIAL INSTRUMENTS AND CAPITAL RISK MANAGEMENT

(Continued)

(a) Categories of financial instruments (continued)

	2012 RMB'000	2011 RMB'000
The Company		
Financial assets		
Available-for-sale investments	**1,000**	1,000
Loan and receivables (including cash and cash equivalents)	**927,814**	1,206,185
Financial assets at fair value through profit or loss	**600,000**	100,000
Financial liabilities		
Amortised cost	**312,497**	288,638

(b) Financial risk management objectives and policies

The main risks arising from the Group's financial instruments are market risk (including interest rate risk, foreign currency risk and other price 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 bank balances. Floating-rate interest income is charged to the consolidated statement of comprehensive income as incurred.

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:

	2012	2011
	RMB'000	RMB'000
Assets		
HKD	–	7

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.

	2012	2011
	RMB'000	RMB'000
Impact of HKD		
Profit or loss#	–	–

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.

5. FINANCIAL INSTRUMENTS AND CAPITAL RISK MANAGEMENT

(Continued)

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

Other price risk

The Group is exposed to equity price risk mainly through its investment. The management manages this exposure by maintaining a portfolio of investments with different risk and return profiles. In addition, the management of the Group would monitor the price risk and will consider hedging the risk exposure should the need arise.

Sensitivity analysis on change in fair value of financial assets at fair value though profit or loss

The sensitivity analyses below have been determined based on the exposure to price risk at the end of the reporting period.

If prices had been 10% higher/lower (2011: 10%):

– post-tax profit for the year ended 31 December 2012 would increase/decrease by RMB60,000,000 (2011: RMB10,000,000). This is mainly due to the changes in fair value of financial assets designated as at fair value through profit or loss investments.

Credit risk

As at 31 December 2012, the Group's and the Company's maximum exposure to credit risk which will cause a financial loss to the Group and the Company 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 and the Company have put in place policies to ensure that sales of products are made to customers with an appropriate credit history and the Group and the Company perform periodic credit evaluation of its customers. The Group's and the Company'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 and the Company'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.

5. FINANCIAL INSTRUMENTS AND CAPITAL RISK MANAGEMENT

(Continued)

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

Credit risk (continued)

Other than concentration of credit risk on liquid funds which are deposited with several banks with high credit ratings, the Group and the Company do 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 and the Company's short, medium and long-term funding and liquidity management requirements. The Group and the Company manage liquidity risk by maintaining adequate reserves, by continuously monitoring forecast and actual cash flows and matching the maturity profiles of financial assets and liabilities.

The following table details the Group's and the Company'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 and the Company can be required to pay. The tables include both interest and principal cash flows.

	Weighted average effective interest rate %	On demand or within 1 year RMB'000	Over 1 year RMB'000	Total undiscounted cash flows RMB'000	Total carrying amount RMB'000
The Group					
As at 31 December 2012					
Non-derivative financial liabilities					
Trade and bills payables	–	217,493	–	217,493	217,493
Other payables and accruals	–	102,210	–	102,210	102,210
		319,703	–	319,703	319,703
As at 31 December 2011					
Non-derivative financial liabilities					
Trade and bills payables	–	142,828	–	142,828	142,828
Other payables and accruals	–	147,165	–	147,165	147,165
Deposits received	–	4,286	–	4,286	4,286
		294,279	–	294,279	294,279

5. FINANCIAL INSTRUMENTS AND CAPITAL RISK MANAGEMENT

(Continued)

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

Liquidity risk (continued)

	Weighted average effective interest rate %	On demand or within 1 year RMB'000	Over 1 year RMB'000	Total undiscounted cash flows RMB'000	Total carrying amount RMB'000
The Company					
As at 31 December 2012					
Non-derivative financial liabilities					
Trade and bills payables	–	211,192	–	211,192	211,192
Other payables and accruals	–	101,305	–	101,305	101,305
		312,497	–	312,497	312,497
As at 31 December 2011					
Non-derivative financial liabilities					
Trade and bills payables	–	118,270	–	118,270	118,270
Other payables and accruals	–	144,309	–	144,309	144,309
Deposits received	–	26,059	–	26,059	26,059
		288,638	–	288,638	288,638

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 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.

(iii) the fair values of other financial assets and financial liabilities are determined in accordance with generally accepted pricing models based on discounted cash flow analysis.

5. FINANCIAL INSTRUMENTS AND CAPITAL RISK MANAGEMENT

(Continued)

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

Fair value of financial instruments (continued)

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 quoted 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).

	31 December 2012			
	Level 1	**Level 2**	**Level 3**	**Total**
	RMB'000	**RMB'000**	**RMB'000**	**RMB'000**
Financial assets				
Financial assets designated as at fair value through profit or loss	**600,000**	**–**	**–**	**600,000**

	31 December 2011			
	Level 1	Level 2	Level 3	Total
	RMB'000	RMB'000	RMB'000	RMB'000
Financial assets				
Financial assets designated as at fair value through profit or loss	100,000	–	–	100,000

Note: The financial assets designated as at fair value through profit or loss for 2011 is restated as level 1 fair value hierarchy.

There were no transfers between Levels 1 and 2 in the both years.

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 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 2012, 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 2012 and 2011 are as follows:

	As at 31 December	
	2012	2011
	RMB'000	RMB'000
Total debt	**–**	–
Total assets	**2,288,547**	1,937,283
Gearing ratio	**N/A**	N/A

6. SEGMENT INFORMATION

Information reported to the Board of Directors of the Company, being the chief operating decision makers, for the purposes of resource allocation and assessment of segment performance focuses on types of goods delivered.

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 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.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2012

6. SEGMENT INFORMATION (Continued)

Revenue from major products

The Group's revenue from its major product is as follows:

	2012 RMB'000	2011 RMB'000
Pharmaceutical products	**2,228,257**	1,626,848

Information about major customers

Included in revenues arising from sales of pharmaceutical products of approximately RMB2,228,257,000 (2011: RMB1,626,848,000) are revenues of approximately RMB491,855,000 (2011: RMB344,252,000) which arose from sales to the Group's largest customer.

Geographical information

The Group only operates in the PRC. The Group's revenue for each of the year ended 31 December 2012 and 2011 is derived from external customers located in the PRC. The non-current assets of the Group are all located in the PRC in each of the year ended 31 December 2012 and 2011.

7. TURNOVER AND OTHER REVENUE

Turnover and other revenue recognised are as follows:

	2012 RMB'000	2011 RMB'000
Turnover		
Sales of manufactured pharmaceutical products	**2,228,257**	1,626,848
Other revenue		
Interest income on bill receivables	**1,683**	855
Interest income on bank deposits	**6,779**	6,287
Interest income on financial assets at fair value through profit or loss	**14,282**	–
Sundry income	**7,134**	1,881
	29,878	9,023
Total revenue	**2,258,135**	1,635,871

7. TURNOVER AND OTHER REVENUE (Continued)

The sales of product mix of the Group are as follows:

	2012 RMB'000	2011 RMB'000
Respiratory and Digestive System Specified Medicine	727,328	444,910
Cephalosporin	998,706	787,719
Others System Specified Medicine	502,223	394,219
	2,228,257	1,626,848

8. FINANCE COSTS

	2012 RMB'000	2011 RMB'000
Bills payables wholly repayable within six months	90	168

9. PROFIT FROM OPERATIONS

Operating profit of the Group was determined after charging/(crediting) the following:

	2012 RMB'000	2011 RMB'000
Raw materials and consumables used	691,440	526,651
Depreciation of property, plant and equipment (Note 21)	24,365	22,265
Amortisation of purchased technical know-how (included in cost of sales) (Note 19)	430	525
Amortisation of prepaid lease payments (Note 23)	413	413
Write-down of obsolete inventories (Note 26)	164	4,104
Impairment loss recognised in respect of trade receivables (Note 28)	1,068	829
Impairment loss recognised in respect of other receivables (Note 29)	1,392	361
Employees benefit expenses (excluding Directors' and supervisors' remuneration)	438,276	172,303
Loss on disposal of property, plant and equipment	1,139	11
Research and development costs	78,061	81,927
Rental expenses	125	–
Advertising costs	3,658	5,072
Auditors' remuneration	600	600
and after crediting:		
Other income		
Waiver of trade payables	1	1,115
Government grant	441	4,871
Penalty income	1,110	1,013
Reversal of obsolete inventories written-down (Note 26)	3,960	3,664
Reversal of impairment loss recognised in respect of trade receivables (Note 28)	283	4,301
Reversal of impairment loss recognised in respect of other receivables (Note 29)	472	650
	6,267	15,614

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 (2011: Nil).

(ii) As described in the paragraph below, the Group is subjected to the PRC enterprise income tax at a rate of 15% (2011: 15%).

During the year ended 31 December 2012, the Company applied as the High and New Technology Enterprise. 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% from 1 January 2012.

(iii) The PRC value-added tax

The Group is subjected to the PRC value-added tax ("VAT") at 17% (2011: 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:

	2012 RMB'000	2011 RMB'000
Current taxation – Enterprise income tax	**77,337**	74,523
Deferred taxation (Note 24)	**708**	832
	78,045	75,355

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:

	2012 RMB'000	2011 RMB'000
Profit before taxation	518,154	502,039
Calculated at a taxation rate of 25% (2011: 25%)	129,539	125,510
Tax effect of income not taxable for tax purpose	(20,511)	(13,978)
Tax effect of expenses not deductible for tax purpose	20,268	14,799
Tax effect of tax concession	(51,251)	(49,508)
Tax effect of share of profit of associate	–	(1,468)
Taxation charge for the year	78,045	75,355

11. DIVIDENDS

A dividend in respect of 2012 of RMB0.3 per share (2011: RMB0.2 per share), amounting to a total dividend of RMB182,880,000 (2011: RMB121,920,000 is to be proposed at the annual general meeting of the Company on 10 June 2013. These consolidated financial statements do not reflect this dividend payable.

	2012 RMB'000	2011 RMB'000
Proposed final dividend of RMB0.3 (2011: RMB0.2) per ordinary share	182,880	121,920

12. EMPLOYEE BENEFIT EXPENSES

	2012 RMB'000	2011 RMB'000
Salaries and wages	430,103	166,109
Pension costs – defined contribution plans	8,173	6,194
	438,276	172,303

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 RMB814 (equivalent to HK$1,000) per month before 1 June 2012 and RMB1,017 (equivalent HK$1,250) per month with effect from 1 June 2012, and thereafter contributions are voluntary.

During the year ended 31 December 2012, the Group has contributed approximately RMB11,382 (2011: RMB9,811) to the MPF Scheme.

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:

	2012	2011
	RMB'000	RMB'000
Basic salaries and allowances	**1,056**	1,056
Retirement benefit costs	**60**	51
	1,116	1,107

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)

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

	2012 RMB'000	2011 RMB'000
Executive Directors		
Liu Baoqi	380	380
Li Minghua	129	127
Liu Zhenhai	104	104
Han Fengsheng	69	67
Chen Yu	69	67
Non-executive Directors		
Yin Chuangui	24	24
Liu Yuxin (resigned on 31 December 2012)	24	24
Independent non-executive Directors		
Foo Tin Chung, Victor	120	120
Fu Hongzheng	24	24
Li Hongjian	24	24
Prof. Chen Yun Zhen (appointed on 31 December 2012)	–	–
Supervisors		
Sun Song	68	67
Guan Yonghua	24	24
Wang Jian	24	24
Song Liangwei	33	31
	1,116	1,107

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	
	2012	2011
Nil – RMB813,537 (equivalent to Nil – HK$1,000,000)	**14**	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 (2011: 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 (2011: one) non-director, highest paid individual during the year are as follows:

	2012 **RMB'000**	2011 RMB'000
Basic salaries and allowances	**621**	618
Retirement benefit costs	**11**	10
	632	628

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

	Number of individuals	
	2012	2011
Nil – RMB813,537(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 (2011: Nil).

(iv) Mr. Liu Baoqi was also the chief executive of the Company during the year ended 31 December 2012 and 2011.

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.

	2012	2011
Profit attributable to owners of the Company (RMB'000)	439,874	426,556
Weighted average number of ordinary shares in issue ('000)	609,600	609,600
Basic and diluted earnings per share (RMB)	0.722	0.700

16. INTERESTS IN SUBSIDIARIES

The Company

	2012 RMB'000	2011 RMB'000
Cost of investments in subsidiaries, unlisted in PRC	101,479	118,979

As at 31 December 2012 and 2011, the Company had interests in the following subsidiaries:

Name of the entity	Form of business structure	Place of incorporation and operation	Paid-up register capital	Proportion of registered capital held by the Company		Proportion of voting power held		Principal activities
				2012	2011	2012	2011	
Sichuan Luoxin Pharmacy Company Limited* (四川羅欣醫葯有限公司) ("Sichuan Luoxin")	Incorporated	PRC	RMB3,000,000	51%	51%	51%	51%	Wholesale of biochemical products and Chinese medicine
Shandong Yuxin Pharmacy Company Limited* (山東裕欣藥業有限公司) ("Shandong Yuxin")	Incorporated	PRC	RMB50,000,000	100%	100%	100%	100%	Wholesale and manufacture of biochemical products and Chinese medicine

16. INTERESTS IN SUBSIDIARIES (Continued)

Name of the entity	Form of business structure	Place of incorporation and operation	Paid-up register capital	Proportion of registered capital held by the Company		Proportion of voting power held		Principal activities
				2012	2011	**2012**	2011	
Shandong Hengxin Pharmacy Company Limited*# (山東恒欣藥業有限公司) ("Shandong Hengxin")	Incorporated	PRC	RMB50,000,000	**100%**	100%	**100%**	100%	Wholesale and manufacture of biochemical products and Chinese medicine
Shandong Louxin Biological Technology Company Limited*^ (山東羅欣生物工程有限公司) ("Shandong Biological")	Incorporated	PRC	RMB22,500,000	**–**	77.78%	**–**	77.78%	Wholesale and manufacture of biochemical products and Chines medicine

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

\# Shandong Hengxin and Shandong Biological were incorporated on 11 April 2011 and 19 December 2011 respectively

^ Shandong Biological was de-registered on 18 September 2012.

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

17. INTEREST IN AN ASSOCIATE

The Group and the Company

	2012 **RMB'000**	2011 RMB'000
Cost of investment in an associate, unlisted in the PRC	**–**	–
Share of post-acquisition profits and other comprehensive income, net of dividends received	**–**	–
	–	–

17. INTEREST IN AN ASSOCIATE (Continued)

During the year ended 31 December 2011, the Company disposed of its interest in the associate to an independent third party at a consideration of RMB27,144,000, which is same as the Company's share of net assets of the associate before disposal. Therefore, there was no gain or loss arising from the disposal.

During the year ended 31 December 2011, 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:

	2012 RMB'000	2011 RMB'000
Total assets	–	–
Total liabilities	–	–
Net assets	–	–
Share of net assets of associate	–	–

17. INTEREST IN AN ASSOCIATE (Continued)

	2012 **RMB'000**	2011 RMB'000
Revenue	**–**	29,027
Profit for the period	**–**	29,372
Share of profit of associate for the period	**–**	5,873
Share of other comprehensive income for the period	**–**	1,620

Note:

During the year ended 31 December 2011, the share of profit of associate and other comprehensive income before disposal was approximately RMB7,493,000. The Company received dividend of RMB5,400,000 from the associate during the year.

18. AVAILABLE-FOR-SALE FINANCIAL ASSETS

The Group and the Company

Available-for-sale investments comprise:

	2012 **RMB'000**	2011 RMB'000
Unlisted securities – Equity securities (Note)	**1,000**	1,000

Note:

The Group holds 10% of the capital of 山東羅欣陽光包裝製品有限公司, a company involved in the production and selling of plastic and packaging materials. The Directors of the Company are of the opinion that no impairment is required at the end of the reporting period.

19. PURCHASED TECHNICAL KNOW-HOW

The Group and the Company

	RMB'000
Cost:	
At 1 January 2011	17,450
Additions	–
At 31 December 2011 and 1 January 2012	**17,450**
Additions	**–**
At 31 December 2012	**17,450**
Accumulated amortisation and impairment:	
At 1 January 2011	16,248
Charge for the year	525
At 31 December 2011 and 1 January 2012	**16,773**
Charge for the year	**430**
At 31 December 2012	**17,203**
Net book value:	
At 31 December 2012	**247**
At 31 December 2011	677

20. PREPAYMENTS TO ACQUIRE TECHNICAL KNOW-HOW

The Group and the Company

As at 31 December 2012 and 2011, the amounts are prepayments to third parties to acquire technical know-how. During the year ended 31 December 2009, amount of RMB2,430,000 was impaired. The Directors of the Company have considered that the amount of the prepayment to acquire technical know-how of RMB2,430,000 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. The Directors of the Company are of the opinion that no further impairment was recognised because the remaining research and development process was considered to be successful and would bring future economic benefit to the Group and the Company.

21. PROPERTY, PLANT AND EQUIPMENT

The Group

	Buildings RMB'000	Plant and machinery RMB'000	Motor vehicles RMB'000	Office equipment RMB'000	Total RMB'000
Cost:					
At 1 January 2011	178,935	141,476	13,749	10,884	345,044
Additions	2,534	2,712	4,150	5,570	14,966
Disposals	(12)	–	–	–	(12)
Transfer from construction–in-progress (Note 22)	250	9,997	–	–	10,247
At 31 December 2011 and 1 January 2012	**181,707**	**154,185**	**17,899**	**16,454**	**370,245**
Additions	**1,873**	**12,844**	**3,060**	**1,602**	**19,379**
Disposals	**(111)**	**(1,302)**	**–**	**–**	**(1,413)**
Transfer from construction-in-progress (Note 22)	**98**	**5,982**	**–**	**2,533**	**8,613**
At 31 December 2012	**183,567**	**171,709**	**20,959**	**20,589**	**396,824**
Accumulated depreciation and impairment:					
At 1 January 2011	14,383	49,200	6,159	7,032	76,774
Charge for the year	4,599	13,767	2,387	1,512	22,265
Written back on disposals	(1)	–	–	–	(1)
At 31 December 2011 and 1 January 2012	**18,981**	**62,967**	**8,546**	**8,544**	**99,038**
Charge for the year	**4,703**	**14,619**	**2,883**	**2,160**	**24,365**
Written back on disposals	**(12)**	**(262)**	**–**	**–**	**(274)**
At 31 December 2012	**23,672**	**77,324**	**11,429**	**10,704**	**123,129**
Net book value:					
At 31 December 2012	**159,895**	**94,385**	**9,530**	**9,885**	**273,695**
At 31 December 2011	162,726	91,218	9,353	7,910	271,207

21. PROPERTY, PLANT AND EQUIPMENT (Continued)

As at 31 December 2012 and 2011, all buildings of the Group are located in the PRC.

Depreciation expense of RMB18,978,000 (2011: RMB15,354,000) have been expensed in cost of sales and RMB5,387,000 (2011: RMB6,911,000) have been included in administrative expenses for the year.

The Company

	Buildings RMB'000	Plant and machinery RMB'000	Motor vehicles RMB'000	Office equipment RMB'000	Total RMB'000
Cost:					
At 1 January 2011	178,935	141,476	13,692	10,803	344,906
Additions	2,534	2,712	3,524	5,551	14,321
Disposals	(12)	–	–	–	(12)
Transfer from construction–in-progress (Note 22)	250	9,997	–	–	10,247
At 31 December 2011 And 1 January 2012	181,707	154,185	17,216	16,354	369,462
Additions	1,873	12,844	3,060	1,515	19,292
Disposals	(111)	(1,302)	–	–	(1,413)
Transfer from construction–in-progress (Note 22)	98	5,982	–	2,533	8,613
At 31 December 2012	183,567	171,709	20,276	20,402	395,954
Accumulated depreciation and impairment:					
At 1 January 2011	14,383	49,200	6,159	7,019	76,761
Charge for the year	4,599	13,767	2,307	1,484	22,157
Written back on disposals	(1)	–	–	–	(1)
At 31 December 2011 and 1 January 2012	18,981	62,967	8,466	8,503	98,917
Charge for the year	4,703	14,619	2,752	2,121	24,195
Written back on disposals	(12)	(262)	–	–	(274)
At 31 December 2012	23,672	77,324	11,218	10,624	122,838
Net book value:					
At 31 December 2012	159,895	94,385	9,058	9,778	273,116
At 31 December 2011	162,726	91,218	8,750	7,851	270,545

22. CONSTRUCTION-IN-PROGRESS

The Group

	RMB'000
At 1 January 2011	52,826
Additions	73,835
Transfer to property, plant and equipment (Note 21)	(10,247)
At 31 December 2011 and 1 January 2012	**116,414**
Additions	**121,577**
Transfer to property, plant and equipment (Note 21)	**(8,613)**
At 31 December 2012	**229,378**

Analysis of construction-in-progress as follows:

	2012	2011
	RMB'000	RMB'000
Construction cost of buildings	**117,253**	63,994
Cost of plant and machinery	**112,125**	52,420
	229,378	116,414

22. CONSTRUCTION-IN-PROGRESS (Continued)

The Company

	RMB'000
At 1 January 2011	18,352
Additions	5,956
Transfer to property, plant and equipment (Note 21)	(10,247)
At 31 December 2011 and 1 January 2012	**14,061**
Additions	**96,896**
Transfer to property, plant and equipment (Note 21)	**(8,613)**
At 31 December 2012	**102,344**

Analysis of construction-in-progress as follows:

	2012	2011
	RMB'000	RMB'000
Construction cost of buildings	**27,893**	3,938
Cost of plant and machinery	**74,451**	10,123
	102,344	14,061

23. PREPAID LEASE PAYMENTS

The Group

Prepaid lease payments represent 48-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 2011	20,513
Amortisation of prepaid lease payments	(413)
At 31 December 2011 and 1 January 2012	**20,100**
Addition of prepaid lease payment	**33,664**
Amortisation of prepaid lease payments	**(413)**
At 31 December 2012	**53,351**

Analysed for reporting purposes as:

	2012 **RMB'000**	2011 RMB'000
Current assets (included in other receivables, deposits and prepayments)	**412**	413
Non-current assets	**52,939**	19,687
	53,351	20,100

	2012 **RMB'000**	2011 RMB'000
Long-term lease	**9,227**	9,420
Medium-term lease	**44,124**	10,680
	53,351	20,100

23. PREPAID LEASE PAYMENTS (Continued)

The Company

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 2011	20,513
Amortisation of prepaid lease payments	(413)
At 31 December 2011 and 1 January 2012	**20,100**
Amortisation of prepaid lease payments	**(413)**
At 31 December 2012	**19,687**

Analysed for reporting purposes as:

	2012 **RMB'000**	2011 RMB'000
Current assets (included in other receivables, deposits and prepayments)	**412**	413
Non-current assets	**19,275**	19,687
	19,687	20,100

	2012 **RMB'000**	2011 RMB'000
Long-term lease	**9,227**	9,420
Medium-term lease	**10,460**	10,680
	19,687	20,100

24. 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% (2011: 25%).

The movements in the deferred tax assets are as follows:

	2012 **RMB'000**	2011 RMB'000
At the beginning of the year	**2,680**	3,512
Deferred taxation charged to the consolidated statement of comprehensive income (Note 10)	**(708)**	(832)
At the end of the year	**1,972**	2,680

	Provisions RMB'000	**Amortisation charge on purchased technical know-how** RMB'000	**Total** RMB'000
At 1 January 2011	2,940	572	3,512
Charged to the consolidated statement of comprehensive income	(720)	(112)	(832)
At 31 December 2011 and 1 January 2012	**2,220**	**460**	**2,680**
Charged to the consolidated statement of comprehensive income	**(584)**	**(124)**	**(708)**
At 31 December 2012	**1,636**	**336**	**1,972**

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

There is no unprovided deferred taxation during the year.

25. GOODWILL

The Group

The carrying amount of goodwill was allocated to cash-generating unit as follows:

	2012 **RMB'000**	2011 RMB'000
Manufacturing and selling of pharmaceutical products	**165**	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 selling 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.

26. INVENTORIES

The Group

	2012	2011
	RMB'000	RMB'000
Raw materials	**61,789**	43,138
Work-in-progress	**31,661**	39,395
Finished goods	**95,451**	70,582
	188,901	153,115
Less: Write down of obsolete inventories	**(557)**	(4,353)
	188,344	148,762

The cost of inventories recognised as expense and included in cost of sales amounted to approximately RMB621,918,000 (2011: RMB547,879,000).

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

	2012	2011
	RMB'000	RMB'000
Balance at the beginning of the year	**4,353**	3,913
Write-down of obsolete inventories during the year	**164**	4,104
Reversal of obsolete inventories written-down	**(3,960)**	(3,664)
Balance at the end of the year	**557**	4,353

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 inventories as at 31 December 2012 and have considered a write-down of obsolete inventories of approximately RMB557,000 (2011: RMB4,353,000) be made in respect of the net realisable value of the inventories.

26. INVENTORIES (Continued)

The Company

	2012 RMB'000	2011 RMB'000
Raw materials	**61,789**	43,138
Work-in-progress	**31,661**	39,395
Finished goods	**93,017**	66,344
	186,467	148,877
Less: Write down of obsolete inventories	**(557)**	(4,353)
	185,910	144,524

The cost of inventories recognised as expense and included in cost of sales amounted to approximately RMB614,341,000 (2011: RMB543,499,000).

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

	2012 RMB'000	2011 RMB'000
Balance at the beginning of the year	**4,353**	3,913
Write-down of obsolete inventories during the year	**164**	4,104
Reversal of obsolete inventories written-down	**(3,960)**	(3,664)
Balance at the end of the year	**557**	4,353

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 Company's inventories as at 31 December 2012 and have considered a write-down of obsolete inventories of approximately RMB557,000 (2011: RMB4,353,000) be made in respect of the net realisable value of the inventories.

27. AMOUNTS DUE FROM SUBSIDIARIES

The Company

	Highest balances during the year RMB'000	2012 RMB'000	2011 RMB'000
Sichuan Luoxin	15,922	**8,556**	15,922
Shandong Hengxin	98,954	**48,849**	98,954
Shandong Yuxin	101,407	**101,407**	69,499
		158,812	184,375

The amounts due are unsecured, interest-free and recoverable on demand.

28. TRADE AND BILLS RECEIVABLES

The Group

	2012 RMB'000	2011 RMB'000
Trade receivables	**286,275**	147,950
Bills receivables	**31,119**	88,590
	317,394	236,540
Less: Provision for impairment loss recognised in respect of trade receivables	**(4,512)**	(3,727)
	312,882	232,813

28. 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:

	2012 RMB'000	2011 RMB'000
1 to 90 days	239,001	136,180
91 to 180 days	65,020	94,386
181 to 365 days	8,861	2,247
	312,882	232,813

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 2012 and 2011 are denominated in RMB.

As at 31 December 2012, amount of approximately RMB87,866,000 was receivable from two connected parties (Note 40). The amounts due are unsecured, interest-free and receivable within 180 days.

As at 31 December 2011, amount of approximately RMB60,288,000 was receivable from three connected parties (Note 40). The amounts due are unsecured, interest-free and receivable within 180 days.

28. TRADE AND BILLS RECEIVABLES (Continued)

(a) Included in the Group's trade and bills receivables balance are debtors with a carrying amount of approximately RMB8,861,000 (2011: RMB2,247,000) which are past due at the reporting date for which the Group has not provided for impairment loss. The Group has 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 does not hold any collateral over these balances.

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

	2012 **RMB'000**	2011 RMB'000
181 to 365 days	**8,861**	2,247

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

	2012 **RMB'000**	2011 RMB'000
Balance at the beginning of the year	**3,727**	7,199
Impairment loss recognised during the year	**1,068**	829
Reversal of impairment loss recognised in respect of trade receivables	**(283)**	(4,301)
Balance at the end of the year	**4,512**	3,727

In determining the recoverability of trade receivables, the Group considers 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.

28. TRADE AND BILLS RECEIVABLES (Continued)

The Company

	2012 RMB'000	2011 RMB'000
Trade receivables	279,600	141,375
Bills receivables	31,119	86,847
	310,719	228,222
Less: Provision for impairment loss recognised in respect of trade receivables	(4,371)	(3,727)
	306,348	224,495

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

	2012 RMB'000	2011 RMB'000
1 to 90 days	232,601	128,084
91 to 180 days	64,987	94,305
181 to 365 days	8,760	2,106
	306,348	224,495

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 2012 and 2011 are denominated in RMB.

As at 31 December 2012, amount of approximately RMB87,866,000 was receivable from two connected parties (Note 40). The amounts due are unsecured, interest-free and receivable within 180 days.

As at 31 December 2011, amount of approximately RMB60,288,000 was receivable from three connected parties (Note 40). The amounts due are unsecured, interest-free and receivable within 180 days.

28. TRADE AND BILLS RECEIVABLES (Continued)

(a) Included in the Company's trade and bills receivables balance are debtors with a carrying amount of approximately RMB8,760,000 (2011: RMB2,106,000) which are past due at the reporting date for which the Company has not provided for impairment loss. The Company has 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 Company does not hold any collateral over these balances.

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

	2012	2011
	RMB'000	RMB'000
181 to 365 days	**8,760**	2,106

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

	2012	2011
	RMB'000	RMB'000
Balance at the beginning of the year	**3,727**	7,199
Impairment loss recognised during the year	**926**	829
Reversal of impairment loss recognised in respect of trade receivables	**(282)**	(4,301)
Balance at the end of the year	**4,371**	3,727

In determining the recoverability of trade receivables, the Company considers 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.

29. OTHER RECEIVABLES, DEPOSITS AND PREPAYMENTS

The Group

	2012 RMB'000	2011 RMB'000
Other receivables and deposits (Note a)	85,834	15,043
Prepayments (Note b)	90,290	90,329
	176,124	105,372
Less: Provision for impairment loss recognised in respect of other receivables	(1,719)	(799)
	174,405	104,573

Note:

(a) Included in other receivables and deposits, a refundable amount of RMB40,000,000 was paid for incorporation of an associate.

(b) 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 RMB38,608,000 (2011: RMB12,109,000), RMB14,160,000 (2011: RMB9,764,000) and RMB37,110,000 (2011: RMB68,569,000) respectively.

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

	2012 RMB'000	2011 RMB'000
Balance at the beginning of the year	799	1,088
Impairment loss recognised during the year	1,392	361
Reversal of impairment loss recognised in respect of other receivables	(472)	(650)
Balance at the end of the year	1,719	799

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 RMB1,719,000 (2011: RMB799,000) 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.

29. OTHER RECEIVABLES, DEPOSITS AND PREPAYMENTS (Continued)

The Company

	2012 RMB'000	2011 RMB'000
Other receivables and deposits (Note a)	84,587	14,961
Prepayments (Note b)	53,030	20,094
	137,617	35,055
Less: Provision for impairment loss recognised in respect of other receivables	(1,719)	(799)
	135,898	34,256

Note:

(a) Included in other receivables and deposits, a refundable amount of RMB40,000,000 was paid for incorporation of an associate.

(b) Prepayments mainly comprised of prepayment of value-added tax, and acquisition of raw materials, packing materials and consumables of approximately RMB38,608,000 (2011: RMB12,109,000), RMB14,118,000 (2011: RMB7,572,000) respectively.

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

	2012 RMB'000	2011 RMB'000
Balance at the beginning of the year	799	1,088
Impairment loss recognised during the year	1,392	361
Reversal of impairment loss recognised in respect of other receivables	(472)	(650)
Balance at the end of the year	1,719	799

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 RMB1,719,000 (2011: RMB799,000) 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.

30. FINANCIAL ASSETS AT FAIR VALUE THROUGH PROFIT OR LOSS

2012

As at 31 December 2012, the financial assets at fair value through profit or loss represent four principal and return-protected financial products ("Financial Products 2012") issued by several financial institutions in the PRC. The Financial Products 2012 were all matured within one year and were classified as current assets.

These financial products were classified as financial assets designated as at financial assets at fair value through profit or loss. The directors of the Company estimated that the fair values of the Financial Products 2012 as at the year end date were approximate to their carrying amounts with reference to the indicative values provided by those financial institutions.

2011

As at 31 December 2011, the financial assets at fair value through profit or loss represent a principal and return-unprotected financial products ("Financial Product 2011") issued by a financial institution in the PRC. The Financial Product 2011 was all matured within one year and was classified as current assets.

These financial products were classified as financial assets designated as at financial assets at fair value through profit or loss. The directors of the Company estimated that the fair value of the Financial Product 2012 as at the year end date was approximate to its carrying amount with reference to the indicative value provided by the financial institution.

31. PLEDGED BANK DEPOSITS/CASH AND BANK BALANCES

The Group and the Company

As at 31 December 2012, bank deposits of the Group approximately RMB101,940,000 (2011: RMB34,481,000) are pledged as collateral for bills payables.

As at 31 December 2012, bank deposits of the Company approximately RMB95,940,000 (2011: RMB12,670,000) are pledged as collateral for bills payables.

The annual effective interest rate on pledged bank deposits is 3.3% (2011: 3.3%).

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.

32. TRADE AND BILLS PAYABLES

The Group

	2012 RMB'000	2011 RMB'000
Trade payables	**115,553**	108,347
Bills payables	**101,940**	34,481
	217,493	142,828

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

	2012 RMB'000	2011 RMB'000
1 to 90 days	**81,279**	79,624
91 to 180 days	**108,370**	36,615
181 to 365 days	**6,278**	5,546
Over 365 days	**21,566**	21,043
	217,493	142,828

Trade and bills payables as at 31 December 2012 and 2011 are denominated in RMB.

The average credit period on trade and bills payables is 90 days. 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.

The Company

	2012 RMB'000	2011 RMB'000
Trade payables	**115,252**	105,600
Bills payables	**95,940**	12,670
	211,192	118,270

32. TRADE AND BILLS PAYABLES (Continued)

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

	2012 RMB'000	2011 RMB'000
1 to 90 days	**75,022**	68,856
91 to 180 days	**108,365**	22,825
181 to 365 days	**6,277**	5,546
Over 365 days	**21,528**	21,043
	211,192	118,270

Trade and bills payables as at 31 December 2012 and 2011 are denominated in RMB.

The average credit period on trade and bills payables is 90 days. Bills payables are all due to mature within 180 days. The Company has financial risk management policies in place to ensure that all payables are paid within the credit timeframe.

33. OTHER PAYABLES AND ACCRUALS

The Group

	2012 RMB'000	2011 RMB'000
Accruals	**21,434**	86,468
Other payables	**80,776**	60,697
Received in advance	**32,228**	24,044
	134,438	171,209

The Company

	2012 RMB'000	2011 RMB'000
Accruals	**21,434**	86,468
Other payables	**79,871**	59,841
Received in advance	**32,228**	24,044
	133,533	170,353

34. 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 2012 and 2011, the Company has not commenced the construction of the new manufacturing plant.

35. SHARE CAPITAL

		Nominal value		
	Number of shares	**Domestic shares**	**H shares**	**Total**
	'000	RMB'000	RMB'000	RMB'000
Registered, issued and fully paid:				
At 31 December 2011 (nominal value of RMB0.10 each)	609,600	44,504	16,456	60,960
At 31 December 2012 (nominal value of RMB0.10 each)	**609,600**	**44,504**	**16,456**	**60,960**

36. 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.

36. RESERVES (Continued)

The Company

The movements of reserves of the Company are as follows:

	Share premium RMB'000	Statutory surplus reserve fund RMB'000 (Note (i))	Statutory public welfare fund RMB'000 (Note (ii))	Retained earnings RMB'000	Total RMB'000
At 1 January 2011	31,139	30,480	6,033	995,477	1,063,129
Profit attributable to owners of the Company	–	–	–	431,379	431,379
Other comprehensive income for the year	–	–	–	–	–
Total comprehensive income for the year	–	–	–	431,379	431,379
Dividend paid	–	–	–	(30,480)	(30,480)
At 31 December 2011 and 1 January 2012	31,139	30,480	6,033	1,396,376	1,464,028
Profit attributable to owners of the Company	–	–	–	435,718	435,718
Other comprehensive income for the year	–	–	–	–	–
Total comprehensive income for the year	–	–	–	435,718	435,718
Dividend paid	–	–	–	(121,920)	(121,920)
At 31 December 2012	**31,139**	**30,480**	**6,033**	**1,710,174**	**1,777,826**
Representing:					
Proposed 2012 final dividends				182,880	
Others				1,527,294	
Retained earnings as at 31 December 2012				1,710,174	

36. RESERVES (Continued)

Notes:

(i) Pursuant to the PRC regulations and the Articles of Association of the Group's entities in the PRC, the entities in the PRC are 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 entity's registered capital. The transfer to this reserve must be made before distribution of dividends to shareholders.

During the year ended 31 December 2012, appropriation of RMB47,000 (2011: RMB69,000) was made by a subsidiary of the Company.

During the years ended 31 December 2012 and 2011, no appropriation has been made by the Company because the statutory surplus reserve fund of the Company has reached 50% of the Company's registered capital.

The statutory surplus reserve fund shall only be used to make good previous years' losses, to expand the entity's production operations, or to increase the capital of the entity. Upon approval by a resolution passed at a shareholders' general meeting, the entity 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 Articles of Association of the Group's entities in the PRC, the contribution to statutory public welfare fund by the entities 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 2012 and 2011.

37. BANKING FACILITIES

The Group had aggregate banking facilities of approximately RMB101,940,000 (2011: RMB34,481,000) which were fully utilised as at 31 December 2012.

As at 31 December 2012, RMB101,940,000 (2011: RMB34,481,000) of the banking facilities were secured by pledged bank deposits of approximately RMB101,940,000 (2011: RMB34,481,000).

38. COMMITMENTS AND CONTINGENCIES

The Group had the following significant capital commitments:

(a) *Operating leases*

At 31 December 2012, the total future minimum lease payments under non-cancellable operating leases in respect of land and buildings are payable as follows:

	2012 RMB'000	2011 RMB'000
Within one year	58	–

The Group leases office premises under operating lease arrangements which are negotiated and fixed for an average term of a year. The lease payments are fixed and pre-determined.

(b) *Capital commitments*

Capital commitments outstanding at 31 December 2012, not provided for in the consolidated financial statements were as follows:

	2012 RMB'000	2011 RMB'000
Contracted but not provided for:		
– Purchase of technical know-how	3,130	4,376
– Purchase of property, plant and equipment	217,023	103,759

39. RELATED PARTY TRANSACTIONS

Key management compensation for the year ended 31 December 2012 and 2011 was disclosed in Note 14(i).

Apart from those as disclosed under Note 29 and elsewhere in the consolidated financial statements, the Group had the following material transactions with related parties during the year:

	2012 **RMB'000**	2011 RMB'000
Sales of finished goods to Luoxin Pharmacy Group Company Limited ("Luoxin Pharmacy Group") (note (i))	**491,855**	344,252
Sales of finished goods to Shandong Luosheng Pharmacy Co., Ltd. ("Shandong Luosheng") (note (ii))	**55,461**	51,664
Sales of finished goods to Shandong Mingxin Pharmacy Co., Ltd. ("Shandong Mingxin") (note (iii))	**27,097**	35,679

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 2012, amount of approximately RMB83,565,000 (2011: RMB47,074,000) due from Luoxin Pharmacy Group is included in trade and bills receivables, the terms of the outstanding balance is set out in Note 29.

(ii) Shandong Luosheng is the fellow subsidiary of which Luoxin Pharmacy Group is holding 51% of the equity interests of Shandong Luosheng. Mr. Liu Baoqi and Mr. Liu Zhenhai are also the directors of Shandong Luosheng. As at 31 December 2012, amount of approximately RMBNil (2011: RMB2,336,000) due from Shandong Luosheng is included in trade and bills receivables, the terms of the outstanding balance is set out in Note 29.

(iii) Shandong Mingxin is the fellow subsidiary of which Luoxin Pharmacy Group is holding 51% of the equity interests of Shandong Mingxin. Mr. Liu Baoqi and Mr. Liu Zhenhai are also the directors of Shandong Mingxin. As at 31 December 2012, amount of approximately RMB4,301,000 (2011: RMB10,878,000) due from Shandong Mingxin is included in trade and bills receivables, the terms of the outstanding balance is set out in Note 29.

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".

40. CONTINGENT LIABILITIES

The Group and the Company had no material contingent liabilities as at 31 December 2012.

41. APPROVAL OF THE CONSOLIDATED FINANCIAL STATEMENTS

The consolidated financial statements were approved and authorised for issue by the Board of Directors on 19 March 2013.

FIVE YEARS FINANCIAL SUMMARY

	For the year ended 31 December				
	2012	2011	2010	2009	2008
	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000
Results					
Turnover	**2,228,257**	1,626,848	1,342,254	907,453	667,792
Cost of sales	**(725,977)**	(624,217)	(591,944)	(479,736)	(351,196)
Gross profit	**1,502,280**	1,002,631	750,310	427,717	316,596
Other revenue	**29,878**	9,023	7,705	3,767	2,613
Other income	**6,267**	15,614	3,303	2,501	2,894
Selling and distribution expenses	**(896,150)**	(403,313)	(218,663)	(79,668)	(48,869)
General and administrative expenses	**(124,031)**	(127,621)	(94,399)	(42,874)	(29,438)
Share of profit of an associate	**–**	5,873	2,672	4,063	3,107
Finance costs	**(90)**	(168)	(174)	(240)	(1,250)
Profit before taxation	**518,154**	502,039	450,754	315,266	245,653
Taxation	**(78,045)**	(75,355)	(67,360)	(46,716)	(62,498)
Profit for the year	**440,109**	426,684	383,394	268,550	183,155
Profit attributable to:					
Equity holders of the Company	**439,874**	426,556	383,122	268,550	183,155
Non-controlling interests	**235**	128	272	–	–
	440,109	426,684	383,394	268,550	183,155
Dividends	**182,880**	121,920	12,192	12,192	12,192
Earnings per share attributable to owners of the Company (RMB)	**0.722**	0.700	0.629	0.441	0.300

FIVE YEARS FINANCIAL SUMMARY

	As at 31 December				
	2012	2011	2010	2009	2008
	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000
Assets & Liabilities					
Total assets	**2,288,547**	1,937,283	1,570,906	1,220,473	681,722
Total liabilities	**(449,608)**	(411,533)	(447,980)	(471,618)	(189,507)
	1,838,939	1,525,750	1,122,926	748,855	492,215
Equity attributable to owners of the Company	**1,837,042**	1,519,088	1,121,392	748,573	492,215
Non-controlling interests	**1,897**	6,662	1,534	282	–
	1,838,939	1,525,750	1,122,926	748,855	492,215