

### **DIRECTORS' REPORT**

The directors present their annual report and the audited financial statements for the year ended December 31, 2001.

### **PRINCIPAL ACTIVITIES**

The Company is an investment holding company. Details of the activities of its subsidiaries are set out in note 41 to the financial statements.

### **MAJOR CUSTOMERS AND SUPPLIERS**

For the year ended December 31, 2001, the aggregate sales attributable to the Group's five largest customers comprised approximately 39% of the Group's total sales and the sales attributable to the Group's largest customer was approximately 14%, being sales to companies, other than members of the group, controlled by the Company's ultimate holding company, Shijiazhuang Pharmaceutical Group Company Limited ("SPG").

The aggregate purchases during the year attributable to the Group's five largest suppliers were less than 30% of the Group's total purchases.

Other than SPG, none of the directors, their associates or any shareholders of the Company which, to the knowledge of the directors, owned more than 5% of the Company's issued share capital, had any beneficial interest in the customers mentioned above.

### **RESULTS AND APPROPRIATIONS**

The results of the Group and appropriations of the Company for the year ended December 31, 2001 are set out in the consolidated income statement on page 17 of the annual report and the accompanying notes to the financial statements.

The directors recommend a final dividend of HK3.6 cents per share.

### **RESERVES**

Details of movements in the reserves of the Group and of the Company during the year are set out in note 29 to the financial statements.

### **PROPERTY, PLANT AND EQUIPMENT**

During the year, the Group incurred costs mainly for the construction of new factory buildings and plant and machinery for the expansion of the production facilities of 7-ACA products and the refinement of production facilities of cefazolin and 7-ACA products. Details of these and other movements in the property, plant and equipment of the Group during the year are set out in note 11 to the financial statements.

### **SHARE CAPITAL, WARRANTS AND SHARE OPTIONS**

Details of movements in the issued share capital, warrants and share options of the Company are set out in notes 26, 27 and 28 to the financial statements, respectively.

**DIRECTORS AND DIRECTORS' SERVICE CONTRACTS**

The directors of the Company during the year and up to the date of this report were:

*Executive directors:*

Cai Dong Chen, *Chairman*

Ding Er Gang

Wang Xian Jun

Wei Fu Min

Liu Yi

(appointed on February 22, 2001)

Qu Ji Guang

(appointed on February 22, 2001)

Yue Jin

(appointed on February 22, 2001)

Wei Guo Ping

(passed away on March 19, 2002)

*Independent non-executive directors:*

Huo Zhen Xing

Lee Ka Sze, Carmelo

Qi Mou Jia

In accordance with the Company's Articles of Association 101, Messrs. Cai Dong Chen, Wang Xian Jun and Qi Mou Jia retire by rotation at the forthcoming annual general meeting and, being eligible, offer themselves for re-election.

The term of office of each independent non-executive director is the period up to his retirement by rotation in accordance with the Company's Articles of Association.

None of the directors being proposed for re-election at the forthcoming annual general meeting has a service contract with the Company or any of its subsidiaries, which is not determinable by the Group within one year without payment of compensation, other than statutory compensation.

**BIOGRAPHICAL DETAILS OF DIRECTORS AND SENIOR MANAGEMENT****CAI Dong Chen**

Appointed as a director of the Company in 1998. Mr. Cai, aged 48, senior engineer, is the Chairman of SPG. Mr. Cai graduated from Hebei Pharmaceutical Finance College, the People's Republic of China (the "PRC") in 1972. He joined Hebei Pharmaceutical Factory ("HPF"), the PRC in 1972 as a technician and was appointed factory manager of HPF in 1984. Mr. Cai has over twenty years of management experience in the pharmaceutical industry.

**DING Er Gang**

Appointed as a director of the Company in 1997. Mr. Ding, aged 41, is an economist. He graduated from Hebei College of Economic, the PRC and joined Hebei Province Municipal Planning Research Centre as an assistant researcher. Mr. Ding is responsible for the overall financial management.

**WANG Xian Jun**

Appointed as a director of the Company in 1994. Mr Wang, aged 39, is a senior engineer. He graduated from Beijing Chemical Industrial College, the PRC in 1987 with a master degree in chemical engineering. Mr. Wang is responsible for liaison with investors and intermediaries.

**BIOGRAPHICAL DETAILS OF DIRECTORS AND SENIOR MANAGEMENT – continued****WEI Fu Min**

Appointed as a director of the Company in 1994. Mr. Wei, aged 55, is a senior engineer. He graduated from Tianjin Industrial College, the PRC in 1970. Mr. Wei has over twenty years of technical and management experience in the pharmaceutical industry. Mr. Wei is responsible for the overall technical and production control of the Group's production.

**LIU Yi**

Appointed as a director of the Company in 2001. Mr. Liu, aged 48, graduated from Beijing University, the PRC in 1980. Mr. Liu has over twenty years of management experience in the pharmaceutical industry.

**QU Ji Guang**

Appointed as a director of the Company in 2001. Mr. Qu, aged 47, has over twenty years of marketing and management experience in the pharmaceutical industry.

**YUE Jin**

Appointed as a director of the Company in 2001. Mr. Yue, aged 38, graduated from Hebei University, the PRC in 1985. Mr. Yue has over fifteen years of product development and project management experience in the pharmaceutical industry.

**HUO Zhen Xing**

Appointed as a non-executive director of the Company in 1994. Mr. Huo, aged 65, was the former head of Industrial and Commercial Bank of China, Hebei Province branch and Shijiazhuang sub-branch.

**LEE Ka Sze, Carmelo**

Appointed as a non-executive director of the Company in 1996. Mr. Lee, aged 42, is a solicitor by profession and is a partner of a Hong Kong law firm.

**QI Mou Jia**

Appointed as a non-executive director of the Company in 1996. Mr. Qi, aged 68, is a senior engineer. He is a former director of State Drug Administration of China ("SDA"). He was the deputy chairman and chairman of SDA in 1978 and 1982-1994 respectively.

**DIRECTORS' INTERESTS IN SECURITIES**

As at December 31, 2001, none of the directors or their associates had any personal, family, corporate or other interest in the ordinary shares of the Company as recorded in the register maintained by the Company pursuant to Section 29 of Hong Kong Securities (Disclosure of Interests) Ordinance (the "SDI Ordinance").

As at December 31, 2001, other than as disclosed in the section "Share Options", none of the directors, the chief executives or their associates had any interests in the securities of the Company or any of its associated corporations as defined in the SDI Ordinance and none of the directors or their spouses, or children under the age of 18, had any right to subscribe for the securities of the Company, or had exercised any such right during the year.

**SHARE OPTIONS**

The Company's Share Option Scheme (the "Scheme") was adopted on May 27, 1994 for the primary purpose of providing incentives to directors and eligible employees, and will expire on May 26, 2004. Under the Scheme, the Company may grant to employees of the Group, including executive directors, options to subscribe for shares in the Company for a consideration of HK\$1 for each lot of share options granted. Option granted should be accepted within 28 days from the date of grant, upon payment of the consideration. The subscription price, subject to adjustment, is the higher of the nominal value of the shares and an amount which is based on 80% of the average of the last dealt prices of the shares of the Company on the five trading days immediately before the option is granted. Options granted are exercisable for a period to be notified by the board of directors to each grantee and in any event such period of time shall not exceed a period of three years commencing on the expiry of six months after the date on which the option is accepted and shall expire at the end of such three year period or May 26, 2004 whichever is earlier.

At December 31, 2001, the number of shares in respect of which options had been granted and remained outstanding under the Scheme was 94,784,000 representing 7.6% of the shares of the Company in issue at that date. The maximum number of shares in respect of which options may be granted cannot exceed 10% of the issued share capital of the Company from time to time.

No employee shall be granted an option which, if exercised in full, would result in such employee becoming entitled to subscribe for such number of shares as, when aggregated with the total number of shares already issued under all the options previously granted to him which have been exercised, and, issuable under all the options previously granted to him which are for the time being subsisting and unexercised, would exceed 25% of the aggregate number of shares for the time being issued and issuable under the Scheme. During the year, the Company received HK\$18 as consideration for share options granted.

The following table discloses movements in the Company's share options during the year and options outstanding at the beginning and the end of the year:

Directors	Date of grant	Exercisable period	Exercise price	Number of share options			
				Outstanding at 1.1.2001	Granted during the year	Lapsed during the year	Outstanding at 12.31.2001
Cai Dong Chen	10.31.1997	5.1.1998 to 4.30.2001	HK\$0.81	1,450,000	–	(1,450,000)	–
	3.27.2000	9.28.2000 to 9.27.2003	HK\$0.62	10,000,000	–	–	10,000,000
	8.15.2001	2.16.2002 to 5.26.2004	HK\$0.61	–	5,000,000	–	5,000,000
Ding Er Gang	10.31.1997	5.1.1998 to 4.30.2001	HK\$0.81	1,450,000	–	(1,450,000)	–
	3.27.2000	9.28.2000 to 9.27.2003	HK\$0.62	5,000,000	–	–	5,000,000
	8.15.2001	2.16.2002 to 5.26.2004	HK\$0.61	–	3,000,000	–	3,000,000
Wang Xian Jun	3.27.2000	9.28.2000 to 9.27.2003	HK\$0.62	5,000,000	–	–	5,000,000
	8.15.2001	2.16.2002 to 5.26.2004	HK\$0.61	–	3,000,000	–	3,000,000
Wei Fu Min	8.15.2001	2.16.2002 to 5.26.2004	HK\$0.61	–	4,304,000	–	4,304,000
Liu Yi	2.19.2000	8.20.2000 to 8.19.2003	HK\$0.67	1,306,000	–	–	1,306,000
	8.15.2001	2.16.2002 to 5.26.2004	HK\$0.61	–	3,000,000	–	3,000,000

**SHARE OPTIONS – continued**

Directors	Date of grant	Exercisable period	Exercise price	Number of share options			
				Outstanding at 1.1.2001	Granted during the year	Lapsed during the year	Outstanding at 12.31.2001
Qu Ji Guang	2.19.2000	8.20.2000 to 8.19.2003	HK\$0.67	1,304,000	–	–	1,304,000
	8.15.2001	2.16.2002 to 5.26.2004	HK\$0.61	–	3,000,000	–	3,000,000
Yue Jin	2.19.2000	8.20.2000 to 8.19.2003	HK\$0.67	1,304,000	–	–	1,304,000
	8.15.2001	2.16.2002 to 5.26.2004	HK\$0.61	–	3,000,000	–	3,000,000
				26,814,000	24,304,000	(2,900,000)	48,218,000
Employees	10.31.1997	5.1.1998 to 4.30.2001	HK\$0.81	25,100,000	–	(25,100,000)	–
	2.19.2000	8.20.2000 to 8.19.2003	HK\$0.67	26,086,000	–	–	26,086,000
	8.15.2001	2.16.2002 to 5.26.2004	HK\$0.61	–	20,480,000	–	20,480,000
				51,186,000	20,480,000	(25,100,000)	46,566,000
				78,000,000	44,784,000	(28,000,000)	94,784,000

The fair value of the options granted in the current year totalled approximately HK\$4,501,000. The following significant assumptions were used to derive the fair values using the Black-Scholes option pricing model:

- 1) an expected volatility of 68%;
- 2) annual dividend of 30% of earnings; and
- 3) Hong Kong Exchange Fund Notes rates of 4.295% and based on the estimated expected life of 2.8 years.

No charge is recognised in the income statement in respect of the value of options granted during the year.

**ARRANGEMENT TO PURCHASE SHARES OR DEBENTURES**

Other than as disclosed above, at no time during the year was the Company or any of its holding companies or its fellow subsidiaries or its subsidiaries a party to any arrangement to enable the directors of the Company to acquire benefits by means of the acquisition of shares in, or debentures of, the Company or any other body corporate.

**DIRECTORS' INTERESTS IN CONTRACTS**

Woo, Kwan, Lee & Lo, a firm of solicitors of which Mr. Lee Ka Sze, Carmelo is a partner, rendered professional services to the Group for which it received normal remuneration.

Other than the above, no contracts of significance subsisted at any time during the year to which the Company, its holding company or any of its subsidiaries or fellow subsidiaries was a party and in which a director of the Company had a material interest, whether directly or indirectly.

**SUBSTANTIAL SHAREHOLDER**

As at December 31, 2001, the register of substantial shareholders maintained by the Company pursuant to Section 16(1) of the SDI Ordinance shows that the following shareholder had an interest of 10% or more in the issued share capital of the Company:

Name of shareholder	Number of ordinary shares of the Company held	Percentage of issued share capital
SPG	651,054,779 <i>(Note)</i>	52.49%

Save as disclosed above, the Company has not been notified of any other interests representing 10% or more of the issued share capital of the Company as at December 31, 2001.

*Note:* Out of the 651,054,779 shares, 25,000,000 shares are held by Mr. Ding Er Gang, an executive director of the Company, as trustee for SPG, 16,729,762 shares are held by China Charmaine Pharmaceutical Company Limited, a wholly-owned subsidiary of SPG.

**CONNECTED TRANSACTIONS**

Details of the discloseable connected transactions during the year are set out in note 40(I) to the financial statements. In the opinion of the independent non-executive directors, the above transactions were entered into by the Group:

- (i) in the ordinary and usual course of the Group's business;
- (ii) on normal commercial terms or on terms that are fair and reasonable so far as the shareholders of the Company are concerned; and
- (iii) in accordance with the terms of the agreements governing such transactions or on terms no less favourable than terms available to or from independent third parties.

**PURCHASE, SALE OR REDEMPTION OF THE COMPANY'S LISTED SECURITIES**

During the year, neither the Company nor any of its subsidiaries purchased, sold or redeemed any of the Company's listed securities.

**DISCLOSURE UNDER PRACTICE NOTE 19 TO THE LISTING RULES**

Pursuant to a term loan agreement, it will be an event of default under the loan agreement if SPG ceases to own more than 40% of the issued share capital of the Company. The outstanding principal of the term loan at December 31, 2001 was HK\$135,000,000 and the last instalment repayment is due on May 21, 2005.

Save as disclosed above, there are no other events which are required to be disclosed by the Company under Practice Note 19 to the Listing Rules.

**CORPORATE GOVERNANCE**

In the opinion of the directors, the Company has complied throughout the year ended December 31, 2001 with the Code of Best Practice as set out in Appendix 14 of the Listing Rules.

**POST BALANCE SHEET EVENT**

Details of a significant post balance sheet event are set out in note 42 to the financial statements.

**AUDITORS**

Messrs. Deloitte Touche Tohmatsu have acted as auditors of the Company since the incorporation of the Company. A resolution will be submitted to the annual general meeting of the Company to re-appoint them.

On behalf of the Board

**CAI Dong Chen**

*Chairman*

Hong Kong, April 22, 2002