



Interim Report
2004



維奧生物科技控股有限公司
Vital BioTech Holdings Limited
(incorporated in the Cayman Islands with limited liability)

HIGHLIGHT

For the 6 months ended
(Unaudited)

	2004	2003
	HK\$'000	HK\$'000
Turnover	149,328	125,312
Profit attributable to shareholders	26,667	24,956
Basic earnings per share	HK1.85 cent	HK2.01 cent
Interim dividend per share	HK0.5 cent	HK1 cent

- Turnover of the Group was approximately HK\$149,328,000, representing an increase of approximately 19%;
- Profit attributable to shareholders was approximately HK\$26,667,000, representing an increase of approximately 6.8%;
- Basic earnings per share was HK1.85 cent; and
- The Directors proposed to pay an interim dividend of HK0.5 cent per share with options for scrip share or partly in cash and partly in scrip share.

BUSINESS REVIEW

I am pleased to announce the unaudited results of the Company and its subsidiaries (collectively the "Group") for the 6 months ended 30 June 2004 ("period under review"). Turnover grew 19% while the profits attributable to shareholders grew 6.8% only to approximately HK\$26.7 million. In the period under review, the Group launched 5 new products. 2 of these were house drug products namely, Depile Capsule and Fenofibrate Chewable Tablet. The other 3 were agency drug products imported from Europe, namely Reparil N Gel and Agiolax Granule of Madaus AG, Germany, and a vaccine for treatment of allergies produced by a Danish pharmaceutical company.

In the last period, the income from sales of Osteoform accounted for more than 90% of the Group's turnover. In this period, new products and Osteoform accounted for 7% and 89% respectively. The production of Opin was suspended to adjust its production techniques and upgrade its formulation. The Group spent HK\$47 million in selling and distribution expenses. About 1/2 of the money was spent directly on advertising and promotional schemes and 1/4 on new products. These expenses increased by 78% on a year-on-year basis and have slowed down the growth of profits attributable to shareholders. The distribution of products sales was as follows:

TURNOVER BY PRODUCT

For the six months of 2004

- Osteoform
- Depile
- Fenofibrate
- Reparil N Gel
- Agiolax
- Vaccine
- Intellectual property
- Other income



For the six months of 2003

- Osteoform
- Opin
- Other income



Product Sales:

The Group saw a need to consolidate its businesses after 2 years of rapid growth. We have steered to a direction of product diversification. 6 products were on the market as compared to 2 in last year. The agency business of distributing prominent imported brands was launched. The growth of our flagship product Osteoform was quite steady at 16% to approximately HK\$133 million when compared to HK\$115 million on a year-on-year basis.

In the previous period, sales of Opin was HK\$9 million but sales in the period under review was put on a halt. The Group initiated an upgrade modification to Opin to implement an advanced and improved formula and production techniques. Opin production was suspended while waiting for approval of this drug supplemental application. The revised Opin new formula will improve the product's future marketability.

For new products: Depile Capsule, an oral herbal drug that relieve symptoms of haemorrhoids, has generated income of approximately HK\$1 million; and Fenofibrate Chewable Tablet, a fibric acid derivative drug for regulating blood lipids, has been launched for market trials. The product required more resources for promotion.

Overseas agency products:

For distribution of imported drugs, the Group started to sell 2 of the proprietary phytopharmaceutical drugs of Madaus AG, Germany, namely: Reparil N Gel, an anti-inflammatory and analgesic drug, and Agiloax granule, a drug that relieve acute and chronic constipation. In the first quarter, Reparil N Gel was imported as finished goods and sold to a distributor at approximately HK\$6 million. In the second quarter, the Group's GMP facilities in China commenced production of Agiolax granule. The first batch of finished goods was sold for about HK\$2.2 million.

Last year, the Group entered into an exclusive distribution arrangement with a major vaccine manufacturer in Europe to sell its allergen vaccines in China. In the first quarter, we planned on the import logistics arrangement. In the second quarter, we sold an initial batch of products and have launched the marketing campaign for the products.

Logistics arrangement for Osteoform

The Group has invested RMB0.8 million to acquire a 40% equity stake in the one and only one export bonded warehouse in the inland region of China. The company is licensed to operate the export bonded warehouse. Commencing the second quarter, Osteoform raw material has been imported directly from the USA to Chengdu City. With these arrangements, we have saved transportation costs and shortened the logistics lead time. The next milestone is to service other exporting entities in the Sichuan Province to extend the source of income.



The production base in Chengdu City, Sichuan Province



In the second quarter of 2004, the new automatic solid dosage workshop was commissioned. The new workshop is designed exclusively for the production of Osteoform. To improve production capacity, efficiency and to maintain a steady supply, the outer packaging procedures have been fully automated. The former Osteoform workshop that was designed for multiple dosage forms have been re-arranged to produce other new products.



The raw material synthesis plant for the Aceclofenac project was awarded a GMP certificate in June 2004 and has commenced production.

The production base in Wuhan City, Hubei Province

Our GMP facilities in Wuhan city comprised a suppository workshop for Opin and newly installed production lines for 4 dosage forms namely granules, capsules, gel and tablets that were designated for the products of Madaus AG, Germany. In the period under review, we have commenced the business operation of Agiolax. It was expected to receive a packaging permit for the product in the year. It was also expected to commence production of another Madaus product, Reparil N Gel, in the near future.

Veterinary Drugs

The Group foresees a revolutionary change in China's veterinary drug market. The strict enforcement of GMP standards would revolutionise the industry and create ample potentials for commercial development. On the other hand, the Group's proprietary technologies could be applied to veterinary drugs. Last year, a wholly-owned subsidiary was formed in Beijing City and local veterinary drug experts have been recruited. The objectives were to explore veterinary drug market in China and to commercialize the PSD technology in veterinary drugs. We expect certain income in the second half of the year. For this project, the Group was optimistic but cautious and exercised conservative financial control to avoid over-expansion.

BUSINESS OUTLOOK

In what remains of the year, the Group will continue to diversify its product portfolio to reduce over-reliance on single product.

Development of Protein Stabilization and Delivery System ("PSD")

We have achieved a number of break through in this period:

We have arrived at a technical cooperation agreement with a renowned international pharmaceutical company on the project of applying PSD to animal vaccines. The Group regards this event as an important first step towards commercializing PSD internationally.

By applying the PSD technology, the Group's R & D center in Australia has successfully manufactured EPO in tablet form ("EPOTAB") at a low cost. The EPOTAB was found to be room temperature stable and able to deliver EPO sublingually to show efficacy in animal models. To advance this innovative technology to clinical trials, the Group is conducting a series of studies to be concluded in 2004, to generate a pre-clinical safety, pharmacokinetic and pharmacodynamic data and to obtain the essential information to apply for ethics approval for clinical trials. A human trial was planned in 2005.

In China, the Group has appointed a government R&D center in Chengdu City in the past and successfully completed an efficacy pilot animal study on sublingual EPO. During the period under review, the group has appointed another military hospital in Beijing City to repeat the experiments and fine tune the study. The objective of these multi-center studies was to examine the biological activity of human recombinant EPO (rhEPO) sublingual tablets in animal bodies in comparison with EPO by injection. This second study proved again in test animal models that sublingual EPO had an ability to stimulate the production of red blood cells (it showed erythropoietic activity). The experiments demonstrated a definite dose-response relationship. The results obtained from these experiments have been consistent across multiple research centers.

In addition, an international pharmaceutical company has expressed an interest in evaluating Receptorase, our product for prevention and treatment of diarrhea in pigs. The first pilot batch has been shipped from Australia to China for sale to trial users. The Group might extend its marketing activity next year.

Progress of Skin Drug Delivery System (“SDDS”)

The Group has joint ventured with Qingdao Growful Pharmaceuticals Group. The construction of the joint venture factory in Qingdao City, China was completed. Two of the production lines are ready. Product registrations are on schedules. Next year, we would expect certain marketing activity will be initiated.



The progress of new products

2 products, Depile Capsule and Fenofibrate Chewable Tablet went on the market for promotional sale. Aceclofenac will be launched in the 3rd quarter.

FINANCIAL REVIEW

CAPITAL STRUCTURE, LIQUIDITY, FINANCIAL RESOURCES AND CURRENCY POLICY

As of 30 June 2004, the Company has issued about 1.5 billion ordinary shares which has accounted for the 170,000,000 shares placed in February 2004, 12,770,000 shares issued for share option exercised and 1,640,000 shares issued as scrip share for the 2003 final dividend.

As of 30 June 2004, market capitalization of the Company was approximately HK\$630 million (31 December 2003: approximately HK\$1,030 million).

As of 30 June 2004, the Group had bank loans of approximately HK\$84 million (31 December 2003: approximately HK\$90.5 million), comprising long-term portion of HK\$10 million (31 December 2003: HK\$12.5 million) and short-term portion of HK\$74 million (31 December 2003: HK\$78 million). Cash on hand amounted to approximately HK\$82.6 million (31 December 2003: HK\$71.7 million).

At present, the Group has obtained total banking facilities of approximately HK\$140 million from banks in HK and China. Unutilised banking facilities amounted to approximately HK\$50 million. The cost of financing was around 4% per annum.

The sales receipts of the Group were denominated in RMB. 72% of the purchases were denominated in USD and 28% in RMB. 29% of the operating expenditures including selling and distribution expenses and administrative expenses were denominated in HK\$, 67% in RMB and 4% in AUD. During the reporting period, the Group was required to settle the purchases in EURO and entered into forward contracts to hedge against foreign currency fluctuation.

For the reporting period, several profit and loss items and ratios were worsened by a higher level of selling and distribution expenses. On a year-on-year basis, turnover has increased, product range has been widened, production cost has been stable and the overall gross profit margin has been maintained. When comparing with the 12 months of 2003, both gross profit margin after selling and distribution expenses and net profit margin dropped by 4%.

Key financial figures and ratios

Profit and loss item:	6 months ended		12 months
	30 June,		
	2004	2003	
Turnover (<i>HK\$'million</i>)	149.3	125.3	280.8
Gross profit margin	71%	71%	72%
Selling and distribution expenses (<i>HK\$'million</i>)	47.2	26.5	73.0
Gross profit margin after selling and distribution expenses	42%	51%	46%
Net profit margin	18%	20%	22%
EBITDA (<i>HK\$'million</i>)	38.0	39.8	86.0
EBITDA/Turnover	25.4%	31.8%	30.6%

Balance sheet item:

The Group policy is to maintain a gross debt equity ratio below 50%. The net debt equity ratio was kept at a very low level. In 1st quarter, 2004, the issues in connection with the replacement of external packing of Osteoform were resolved. In 2nd quarter, sales have been picking up. The average trade receivable turnover day was maintained at 3 months. Inventory (excluding goods in transit) average turnover day increased from 3 months for last year to 5 months for the period. The longer stock turnover day was attributable to 2 reasons: Firstly, Agiolax raw materials amounting to EURO 1.8 million were imported from Madaus AG, Germany by end of last year for the purpose of manufacturing in our production lines in Wuhan City. However, the production lines were not granted the GMP certificates until the 2nd quarter and sales of Agiolax did not take place until June. Secondly, in 2nd quarter, the Group increased the purchase volume of Osteoform raw materials to accommodate the increasing sales volume. The Group expected that the sales momentum in the second half year would gradually reduce the inventory average turnover day.

	As at 30 June 2004 HK\$ million	As at 31 December 2003 HK\$ million
Balance sheet item:		
Short-term bank loans	75.2	78.8
Long-term bank loans	10.1	11.7
Cash on hand	82.6	71.7
Bank loans net of cash on hand	2.7	18.7
Net tangible assets	321.7	194.2
Debt equity ratio (gross)	26.5%	46.6%
Debt equity ratio (net)	0.8%	9.6%
Average trade receivable turnover day	91 days	76 days
Average inventory turnover day	146 days	84 days

Due to the suspension of Opin production, the Group has made provision for bad and doubtful debt and provision for inventories for HK\$1.17 million and HK\$0.96 million respectively.

As of 30 June 2004, the Group had HK\$14.1 million in cash, HK\$5.6 million in securities investment and HK\$14.3 million in fixed assets pledged as collateral to banks.

The usage of proceed from placement

In February, 2004, 170 million ordinary shares of the Company were placed and a net proceed of HK\$119 million was raised. The usage of proceed was as follows:

Projects	Usage as announced HK\$ million	Actual progress of usage HK\$ million
2 projects of sale and distribution of products of European pharmaceutical companies	48	6
1 project of sale and distribution of health supplements of an Australian company	22	10
Research and development of Erythropoietin (EPO) sublingual tablet	18	1
Installation of production lines in Wuhan City	16	16
Working capital	15	20
	<hr/>	<hr/>
Total	119	53

PROPOSED DIVIDEND AND CLOSURE OF REGISTER OF MEMBERS

The Directors proposed to pay an interim dividend of HK0.5 cent per share to the shareholders whose names appeared on the register of members on 10 September 2004. The interim dividend will be payable on 8 October 2004. In addition, pursuant to a resolution of the Directors on 16 August 2004, shareholders may elect to receive the proposed interim dividend in the form of fully paid shares of the Company, or partly in shares and in cash. The holder of every 75 shares will be entitled to one fully paid share of the Company as scrip dividend. Details of the scrip dividend scheme will be sent in a separate circular to those qualified shareholders.

Should all eligible shareholders elect to receive the interim dividend in cash or in the form of fully paid shares of the Group, the effect of the interim dividend herein would be payment of approximately HK\$7.5 million or an additional issue of approximately 19,991,000 fully paid shares of the Company.

The Register of Members of the Company will be closed from 6 September 2004 to 10 September 2004, both days inclusive, during which period no transfer of shares will be effected. In order to qualify for the above-mentioned dividend, all transfers accompanied with relevant share certificates must be lodged with the Company's share registrar, Computershare Hong Kong Investor Services Limited at Rooms 1712-1716, Hopewell Centre, 183 Queen's Road East, Hong Kong not later than 4:00 on 3 September 2004 (Friday).

EMPLOYEE INFORMATION

As at 30 June 2004, the Group had 1,295 employees, comprising 47 in research and development, 300 in production, 821 in sales and distribution, and 127 in general administration and finance. 1,274 of these employees were located in China, 6 in Australia, 15 in Hong Kong and Macau.

Employee remuneration, bonus, share option scheme and training are commensurate with performance and comparable to market rate. Total staff costs for the reporting period amounted to approximately HK\$16 million.

UNAUDITED INTERIM RESULTS:
Condensed Consolidated Profit and Loss Account

(Unaudited)
Six months ended
30 June

	Note	2004 HK\$'000	2003 HK\$'000
Turnover	2	149,328	125,312
Cost of sales		(43,881)	(36,517)
Gross profit		105,447	88,795
Other revenues		5,088	2,105
Selling and distribution expenses		(47,236)	(26,484)
Administrative expenses		(32,821)	(29,511)
Operating profit	3	30,478	34,905
Finance costs		(1,711)	(2,908)
Profit before taxation		28,767	31,997
Taxation	4	(2,399)	(306)
Profit after taxation		26,368	31,691
Minority interests		299	(6,735)
Profit attributable to shareholders		26,667	24,956
Dividend	5	HK0.5 cent	HK1 cent
Earnings per share-basic	6	HK1.85 cent	HK2.01 cent
Earnings per share-diluted	6	HK1.83 cent	HK1.97 cent

Condensed Consolidated Balance Sheet

	Note	(Unaudited) 30 June 2004 HK\$'000	(Audited) 31 Dec 2003 HK\$'000
Non-current assets			
Intangible assets	7	43,069	42,059
Fixed assets	8	198,087	159,907
Investment securities – guaranteed return	9	5,616	5,616
Investment in joint venture and associated companies		6,418	–
		253,190	207,582
Current assets			
Inventories		49,843	38,670
Trade receivables, other receivables, prepayments and deposits	10	124,972	81,290
Bill of exchange receivables from banks		9,541	–
Other investment		191	151
Bank balances and cash			
– pledged		14,163	9,658
– non-pledged		66,747	62,105
		265,457	191,874
Current liabilities			
Trade payables, accrued charges and other payables	11	67,892	40,580
Amounts due to a minority shareholder of subsidiaries		–	228
Value added tax payable		27	1,734
Income tax payable		751	106
Current portion of long-term liabilities		3,120	21,988
Short-term bank loans		63,656	75,637
Trust receipt loans		6,765	–
		142,211	140,273

	Note	(Unaudited) 30 June 2004 HK\$'000	(Audited) 31 Dec 2003 HK\$'000
Net current assets		<u>123,246</u>	<u>51,601</u>
Total assets less current liabilities		<u>376,436</u>	<u>259,183</u>
Representing:			
Share capital	12	14,993	13,149
Reserves	13	342,302	200,715
Proposed dividend	13	<u>7,496</u>	<u>22,382</u>
Shareholders' fund		364,791	236,246
Minority interests		1,505	1,803
Non-current liabilities			
Long-term liabilities		<u>10,140</u>	<u>21,134</u>
		<u>376,436</u>	<u>259,183</u>

Condensed Consolidated Cash Flow Statement**(Unaudited)**
Six months ended
30 June

	2004 HK\$'000	2003 <i>HK\$'000</i>
Net cash inflow/(outflow) from operating activities	(3,139)	20,010
Net cash used in investing activities	(66,742)	(16,289)
Net cash from financing activities	74,523	1,374
	<hr/>	<hr/>
Increase in cash and cash equivalents	4,642	5,095
Cash and cash equivalents at beginning of period	62,105	57,976
	<hr/>	<hr/>
Cash and cash equivalents at end of period	66,747	63,071
	<hr/>	<hr/>

Condensed Consolidated Statement of Changes in Equity**(Unaudited)**
Six months ended
30 June

	2004 HK\$'000	2003 <i>HK\$'000</i>
Total equity as at 1 January	236,246	176,559
Exchange differences arising on translation of the accounts of subsidiaries not recognized in the consolidated profit and loss account	-	(315)
Profit for the period	26,667	24,956
Dividends	(22,409)	(12,273)
Issue of shares by placement	122,400	-
Share issue expenses	(3,838)	-
Issue of shares on exercise of share options	4,371	-
Issue of shares for scrip dividend	1,354	10,023
	<hr/>	<hr/>
Total equity as at 30 June	364,791	198,950
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NOTES TO THE CONDENSED ACCOUNTS

1. Basis of Preparation and Principal Accounting Policies

The unaudited consolidated accounts for the six months ended 30 June 2004 have been prepared in accordance with Statement of Standard Accounting Practice 25 "Interim Financial Reporting" issued by the Hong Kong Society of Accountants and Appendix 16 of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited.

The consolidated profit and loss account should be read in conjunction with the 2003 annual accounts.

Certain comparative figures have been reclassified to conform with the current period's presentation.

2. Turnover

The Group is principally engaged in biotechnology research, manufacturing and trading of pharmaceutical products. Turnover represents invoiced sales net of return goods, discounts allowed, sales taxes or value added taxes, where applicable.

The Group's revenue, expenses, assets, liabilities and capital expenditure are primarily attributable to the trading and manufacturing of pharmaceutical products. The Group's principal market is in Mainland China.

Neither the business segment of the licensing of the Group's technology nor the geographical segment in other country are of a sufficient size to be reported separately.

3. Operating Profit

Operating profit is stated after crediting and charging the following:

	Six months ended 30 June	
	2004 HK\$'000	2003 HK\$'000
Crediting:		
Amortisation of negative goodwill	19	19
Foreign exchange differences, net	301	1,783
Government grant	4,139	-
Charging:		
Amorisation of goodwill	2,147	321
Amorisation of patents	182	117
Amorisation of developments costs	160	28
Depreciation of fixed assets	4,816	4,519
Research and development costs	1,079	1,797
Provision for bad and doubtful debt	1,227	-
Provision for inventories	492	-

4. Taxation

	Six months ended 30 June	
	2004 HK\$'000	2003 HK\$'000
Current Taxation		
Hong Kong profits tax	-	-
Mainland China taxation	2,399	198
Deferred taxation	-	108
	<hr/> 2,399 <hr/>	<hr/> 306 <hr/>

No Hong Kong profits tax has been provided for the period as there was no assessable profit.

In accordance with the approval documents of relevant local tax bureaus, three subsidiaries operating in mainland China are entitled to exemption from enterprise income tax in the first two years from the first profit-making year and 50% reduction in the subsequent three years. A subsidiary was in the first year of exemption. A second subsidiary was in the first year of 50% reduction while the third subsidiary was in the third year of 50% reduction for the reporting period.

Other subsidiaries in mainland China was in loss-making position for the current and the previous periods and accordingly did not have any taxable income.

The subsidiary operating in Macao is exempted from income tax in Macao.

No Australian income tax has been provided as the subsidiaries operating in Australia had no estimated net assessable profit for the current and previous periods.

5. Dividend

The Board proposed an interim dividend of HK0.5 cent for the reporting period (6 months ended 30 June 2003: HK1 cent). The shareholders can opt to receive scrip share, or partly in scrip share and partly in cash.

6. Earnings Per Share

The calculation of the basic earnings per share is based on the profit attributable to shareholders of approximately HK\$26,667,000 (2003: HK\$24,956,000) and weighted average of approximately 1,442,212,000 (2003: 1,240,084,000) shares in issue during the period.

The calculation of diluted earnings per share is based on the profit attributable to shareholders of approximately HK\$26,667,000 (2003: HK\$24,956,000) and approximately 1,453,243,000 (2003: 1,268,560,000) shares which are the weighted average number of approximately 1,499,287,194 (2003: 1,277,462,169) shares in issue plus the weighted average of shares deemed to be issued at no consideration if all outstanding dilutive share options had been exercised during the period.

7. Intangible Assets

	Goodwill <i>HK\$'000</i>	Negative Goodwill <i>HK\$'000</i>	Patents <i>HK\$'000</i>	Development costs <i>HK\$'000</i>	Total <i>HK\$'000</i>
Net book value, as at 1 Jan 2004	37,977	(122)	2,582	1,622	42,059
Additions	–	–	105	3,375	3,480
Amortisation for the period	(2,147)	19	(182)	(160)	(2,470)
Net book value, as at 30 June 2004	<u>35,830</u>	<u>(103)</u>	<u>2,505</u>	<u>4,837</u>	<u>43,069</u>

8. Additions to Fixed Assets

During the period, the Group spent approximately HK\$42 million (2003: HK\$65 million) on additions to fixed assets to upgrade its manufacturing capacities, and constructing new manufacturing plant and R&D centers.

9. Investment securities

	As at 30 June 2004 HK\$'000	As at 31 Dec 2003 HK\$'000
Unlisted investments in guaranteed funds, at cost	4,056	4,056
Unlisted investments in certificates of deposits, at cost	1,560	1,560
	<u>5,616</u>	<u>5,616</u>

10. Trade receivables, prepayment, deposits and other receivables

The Group's sales for the period are on open account terms and letters of credit. While the Group's sales for the previous period were mainly on open account terms.

The Group normally grants to its customers a credit period ranging from 90 days to 120 days. For some of the new products, the credit period can range from 150 days to 180 days. These are subject to periodic review by management.

The aging analysis of the trade receivable is as follows:

	As at 30 June 2004 HK\$'000	As at 31 Dec 2003 HK\$'000
Trade receivables		
Within 30 days	79,359	25,212
31-60 days	109	14,625
61-90 days	873	7,589
Over 90 days	2,023	10,604
	<hr/>	<hr/>
Prepayment, deposits and other receivables	82,364	58,030
	42,608	23,260
	<hr/>	<hr/>
	124,972	81,290
	<hr/>	<hr/>

11. Trade Payables, accrued charges and other payables

The aging analysis of the trade payable is as follows:

	As at 30 June 2004 HK\$'000	As at 31 Dec 2003 HK\$'000
Trade payables		
Within 30 days	11,320	18,720
31-60 days	2,457	1,151
61-90 days	94	59
Over 90 days	17,301	255
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Accrued charges and other payables	31,172	20,185
	36,720	20,395
	<hr/>	<hr/>
	67,892	40,580
	<hr/>	<hr/>

12. SHARE CAPITAL

Authorised:

	Number of share	Par value per share HK\$	Amount HK\$'000
As at 31 Dec 2003 and 30 June 2004	<u>50,000,000,000</u>	0.01	<u>500,000</u>

Issued and fully paid

	Number of share	Par value per share HK\$	Amount HK\$'000
As at 1 Jan 2004	1,314,876,127	0.01	13,149
Issue of shares by placement	170,000,000	0.01	1,700
Issue of shares on exercise of share options	12,770,000	0.01	128
Issue of shares for scrip dividends	<u>1,641,067</u>	0.01	<u>16</u>
As at 30 June 2004	<u>1,499,287,194</u>		<u>14,993</u>

13. RESERVES

	Share premium HK\$'000	Exchange translation reserve HK\$'000	Reserve fund HK\$'000	Enterprise development fund HK\$'000	Retained profits HK\$'000	Total HK\$'000
At 1 January 2003	83,690	30	1,231	616	78,719	164,286
Exchange translation differences	-	(494)	-	-	-	(494)
Transfer of reserves	-	-	7,261	-	(7,261)	-
Premium on issue of shares on exercise of share options	3,036	-	-	-	-	3,036
Profit for the year	-	-	-	-	61,142	61,142
2002 final dividends	-	-	-	-	(12,273)	(12,273)
2003 interim dividends	-	-	-	-	(12,775)	(12,775)
Premium on issue of shares for scrip dividends	20,175	-	-	-	-	20,175
At 31 December 2003	106,901	(464)	8,492	616	107,552	223,097
At 1 January 2004	106,901	(464)	8,492	616	107,552	223,097
Premium on issue of shares on exercise of share options	4,244	-	-	-	-	4,244
Premium on issue of shares for scrip dividends	1,337	-	-	-	-	1,337
Premium on issue of shares by placement	120,700	-	-	-	-	120,700
Share issue expenses	(3,838)	-	-	-	-	(3,838)
2003 final dividend	<i>Note (a)</i>	-	-	-	(22,409)	(22,409)
Profit for the period	-	-	-	-	26,667	26,667
At 30 June 2004	229,344	(464)	8,492	616	111,810	349,798
Representing:						
Reserves	229,344	(464)	8,492	616	104,314	342,302
2004 interim dividend proposed	<i>Note (b)</i>	-	-	-	7,496	7,496
	229,344	(464)	8,492	616	111,810	349,798

Note (a): The 2003 final dividend of approximately HK\$22,409,000 was settled partly by cash of HK\$21,055,000 and partly by scrip shares of HK\$1,354,000.

Note (b): In the Directors Meeting held on 16 August 2004, the Directors have resolved the payment of an interim dividend of HK0.5 cent for the six months ended 30 June 2004 to the shareholders whose names appeared on the register of members on 10 September 2004.

14. CONTINUING CONNECTED TRANSACTIONS

A subsidiary of the Group purchased raw materials from Pharmco International Inc. ("Pharmco") amounted to approximately HK\$32,142,000 during the six months ended 30 June 2004 (six months ended 30 June 2003: HK\$28,758,000), a company wholly owned by the minority shareholders of a subsidiary, at prices and terms as set out in the agreement entered into between the Group and Pharmco.

As at 30 June 2004, short term bank loans of approximately HK\$9,434,000 (31 December 2003: HK\$9,434,000) of Vital Pharmaceuticals (Sichuan) Co., Ltd., a 100% owned subsidiary of the Company, were guaranteed by Wuhan Weiao Pharmaceuticals Co., Ltd., a 95% owned subsidiary of the Company. At the same date, short term bank loan of approximately HK\$2,830,000 (31 December 2003: HK\$12,264,000) of Wuhan Weiao Pharmaceuticals Co., Ltd. were guaranteed by Vital Pharmaceuticals (Sichuan) Co., Ltd..

15. COMMITMENTS

Capital commitments for construction in progress, fixed assets and other investments are as follow:

	As at 30 June 2004 HK\$'000	As at 31 Dec 2003 HK\$'000
Authorised but not contract for	14,011	23,758
Contracted but not provide for	22,461	39,566
	<u>36,472</u>	<u>63,324</u>

16. PLEDGE OF ASSETS

As at 30 June 2004, the net book values of the fixed assets, cash and securities investment pledged as security for the Group's long term and short term bank loans amounted to approximately HK\$14,330,000 (31 December 2003: HK\$46,341,000), bank balances of the Group approximately HK\$14,163,000 (31 December 2003: HK\$9,658,000) and securities investment HK\$5,616,000 (31 December 2003: HK\$5,616,000) respectively, together with corporate guarantees of the Company, for credit facility granted by banks. Such facilities were utilised to the extent of approximately HK\$70 million.

DIRECTOR'S AND CHIEF EXECUTIVE'S INTEREST IN SHARES OF LISTED CORPORATION

The interests and short positions of the Directors in the share capital of the Company and its associated corporations (within the meaning of the Securities and Future Ordinance ("SFO")) which will have to be notified to the Company and the Stock Exchange pursuant to Divisions 7 and 8 of Part XV of the SFO (including interests and short positions which they are taken or deemed to have under such provisions of the SFO), or which will be required pursuant to section 352 of the SFO to be entered in the register referred to therein, or which will be required to be notified to the Company and the Stock Exchange pursuant to the Model Code for Securities Transactions by Directors of Listed Companies in the Listing Rules, are as follows:

Ordinary shares of HK\$0.01 each in the Company

Name of Director	Company/name of associated corporation	Capacity	Number and class of securities (Note 1)	Percentage shareholding in the same class of securities
Mr. Ko Sai Ying, Thomas ("Mr. Ko")	Company	Beneficial owner	52,303,991 (L)	3.489%
Mr. Au Yeung Ping Yuen, Terence ("Mr. Au Yeung")	Company	Beneficial owner	7,856,248 (L)	0.524%
Mr. Liu Jin, James ("Mr. Liu")	Company	Beneficial owner	14,630,400 (L)	0.976%
Mr Shen Song Qing ("Mr. Shen")	Company	Beneficial owner	18,000,000 (L)	1.2%
Mr Jin Wei ("Mr. Jin")	Company	Beneficial owner	12,000,000 (L)	0.8%
Mr Liao Yong Guang ("Mr. Liao")	Company	Beneficial owner	1,000,000 (L)	0.07%
Mr. Tao Lung ("Mr. Tao")	Company	Beneficial owner	110,891,648 (L)	7.396%
	Company	Interest of a controlled corporation (Note 2)	563,876,940 (L)	37.61%
	Perfect Develop Holding Inc. ("Perfect Develop")	Beneficial owner	49 ordinary shares of US\$1 each (L)	49%

Notes:

1. The letter "L" stands for the Director's long position in such securities.
2. The interest in the shares are held by Perfect Develop. The entire issued share capital of Perfect Develop is beneficially owned as to 33% by Mr. Ko, 6% by Mr. Au Yeung, 12% by Mr. Liu and 49% by Mr. Tao. Accordingly, Mr. Tao is deemed to be interested in all the Shares which Perfect Develop is interested by virtue of the SFO.

DIRECTORS' AND CHIEF EXECUTIVES' RIGHT TO SUBSCRIBE FOR SHARES

In the Reporting Period, none of the Directors or chief executive or their respective spouse and children under 18 of age was granted any options to subscribe for shares of the Company, nor had exercised such rights.

SHARE OPTION SCHEME

The share option scheme dated 26 January 2002 was replaced by a new share option scheme adopted on 23 July 2003. The Directors may grant options to the eligible person for subscription of shares of the Company. The limit of the Scheme is 120,000,000 shares.

First phase:

On 21 June 2002, the Board allotted share options to employees of the Group and two customers to subscribe for 30,000,000 shares of the Company at an exercise price of HK\$0.39 each.

Those who were granted with the options can exercise their rights in multiple periods where applicable commencing 16 August 2002 to 6 February 2012 as follows:–

From 16 August 2002 to 6 February 2012 – approximately 6,850,000 shares

From 1 January 2003 to 6 February 2012 – approximately 8,280,000 shares

From 1 January 2004 to 6 February 2012 – approximately 6,510,000 shares

From 1 January 2005 to 6 February 2012 – approximately 8,360,000 shares

Among the grantees in this grant of share options, 108 of them are full-time employees of the Company and an aggregate of 21,100,000 options were granted to them; 29 of them are staff of major customers of the Company and an aggregate of 8,900,000 options are granted to them. During the Reporting period, 2,990,000 options granted were exercised and no option was forfeited or cancelled. At 30 June 2004, 18,650,000 share options remained outstanding and exercisable under the Scheme.

Second phase:

On 28 February 2003, the Board allotted share options to three directors of certain subsidiaries of the Group to subscribe for 19,800,000 shares of the Company at an exercise price of HK\$0.24 each. The grantees are entitled to exercise the subscription rights on or before 6 February 2012.

On 15 January 2004, 6,600,000 options granted were exercised. The closing price per share on the date when the options were exercised was HK\$0.66. Including the options exercised last year, this phase was exercised in full.

Third phase:

On 29 September 2003, the Directors granted options to subscribe for an aggregate of 28,500,000 shares of the Company, with an exercise price calculated in accordance with the provisions of the Scheme at HK\$0.51 per share. Those who were granted with the options can exercise their rights in multiple periods starting from 16 August 2002 to 6 February 2012 as below:

From 2 January 2004 to 6 February 2012 – approximately 8,990,000 shares

From 2 July 2004 to 6 February 2012 – approximately 19,510,000 shares

Among the grantees in this grant of share options, 14 of them are full-time employees of the Company and an aggregate of 16,595,000 options were granted to them; 5 of them are directors of certain subsidiaries of the Group and an aggregate of 12,405,000 options are granted to them; and one of them is consultant of a wholly owned subsidiary and 1,000,000 options are granted. During the Reporting period, 3,180,000 options granted were exercised and no option was forfeited or cancelled. At 30 June 2004, 5,810,000 share options remained outstanding and exercisable under the Scheme.

Valuation of the options granted under the Scheme:

The Company adopted Black-Scholes Options Pricing Model to calculate the value of share options.

First phase

For share options to subscribe for 30,000,000 shares granted on 21 June 2002 with an exercise price of HK\$0.39 each, the fair value of the options was HK\$0.25 at the date of grant with assumptions as follows:

1. Using the annual exchange fund notes interest rate of 1.57% as the risk-free interest rate;
2. The expected life is 9.5 years;
3. The expected volatility is 60.16% during the period from 7 February 2002, being the listing day of the Company, to 20 June 2002;
4. No expected dividend as the Company is newly listed.

Second phase

For share options to subscribe for 19,800,000 shares granted on 28 February 2003 with an exercise price of HK\$0.24 each, the fair value of the share options was HK\$0.15 at the date of grant with assumptions as follows:

1. Using the annual exchange fund notes interest rate of 1.9% as the risk-free interest rate;
2. The expected life is 9 years;
3. The expected volatility is 54.66% during the period from 7 February 2002, being the date of the listing of the Shares, to 28 February 2003; and
4. No expected dividend as the Company has a track record of dividends for only 1 year.

Third phase

For share options to subscribe for 28,500,000 shares granted on 29 September 2003 with an exercise price of HK\$0.51 each, the fair value of the share options was HK\$0.17 at the date of grant with assumptions as follows:

1. Using the annual exchange fund notes interest rate of 1.68% as the risk-free interest rate;
2. The expected life is 8.5 years;
3. The expected volatility is 48.16% during the period from 30 September 2002 to 29 September 2003; and
4. Expected annual dividend yield of the Company is 3.9%.

Note: The value of the share options is subject to a number of assumptions and with regard to the limitation of the model. Therefore the value may be subjective and difficult to determine.

Other share options

On 22 September 2003, the Group entered into an agreement to acquire the remaining 15% minority interest of the subsidiary, Vital Pharmaceuticals (Sichuan) Co Ltd. The remaining monetary considerations of the acquisition amounting to approximately HK\$18.9 million will be settled at the sole option of the Company, either in cash or in new ordinary share of the Company. On or before the following dates, the Company may opt to pay cash or to issue new ordinary shares by serving a notice to the seller (the "Notice"):

- 22 September 2004: HK\$9,433,962; and
- 22 March 2005: HK\$9,433,962

The number of option share is calculated at a price that is equal to the higher of the average 30 day closing price of the Company's share on the Stock Exchange immediate prior to the date of the Notice and HK\$0.46 pre share. The maximum number of option share to be issued if based on HK\$0.46 per share will be 41,017,226. A conditional approval has been obtained from the Stock Exchange for the listing of the option shares.

SUBSTANTIAL SHAREHOLDERS

As at 30 June 2004, according to the register of members kept by the Company pursuant to section 336 of the SFO and so far as is known to, or can be ascertained after reasonable enquiry by the Directors, the following persons/entities had an interest or short position in the Shares and underlying Shares which would fall to be disclosed to the Company under the provisions of Divisions 2 and 3 of Part XV of the SFO, or, directly, or indirectly, interested in 5% or more of the nominal value of any class of share capital carrying rights to vote on all circumstances at general meetings of the Company:

Name	Company/Name of Group member		Capacity	Number of shares (Note 1)	Approximate percentage of shareholding
Perfect Develop (Note 2)	Company	Beneficial owner		563,876,940 (L)	37.61%
Mr. Tao (Note 3)	Company	Beneficial owner		110,891,648 (L)	7.396%
		Interest of a controlled corporation		563,876,940 (L)	37.61%
Ms. Li Chun Yi (Note 4)	Company	Interest of spouse		674,768,588 (L)	45.006%

Notes:

- The letter "L" denotes the person's/ entity's long position in the shares.
- The entire issued share capital of Perfect Develop is owned as to 49% by Mr. Tao, 33% by Mr. Ko, 6% by Mr. Au Yeung and 12% by Mr. Liu respectively. All of Mr. Tao, Mr. Ko, Mr. Au Yeung and Mr. Liu are founders of the Group.
- Mr. Tao owns in aggregate 49 shares in, representing approximately 49% of the issued share capital of Perfect Develop. Accordingly, Mr. Tao is deemed, by virtue of the SFO, to be interested in all the Shares in which Perfect Develop is interested, amounting to 563,876,940 Shares. Together with 110,891,648 Shares registered in his own name, Mr. Tao is deemed, by virtue of the SFO, to be interested in, 674,768,588 Shares in aggregate, amounting to approximately 45.006% of the issued share capital of the Company as at 30 June 2004.
- Ms. Li Chun Yi is the wife of Mr. Tao and is taken to be interested in the Shares in which Mr. Tao is interested by virtue of the SFO.

AUDIT COMMITTEE

The audit committee has reviewed the accounting principles and practices adopted by the Group and discussed auditing, internal control and financial reporting matters with the management. The Group's financial statements for the six months ended 30 June 2004 have been reviewed by the audit committee, who are of the opinion that such statements comply with the applicable accounting standards, and the Rules Governing the Listing of Securities (the "Listing Rules") of the Hong Kong Stock Exchange and legal requirements, and that adequate disclosures have been made. At present, the Committee has three members, Messrs. Lui Tin Nang and Lee Kwong Yiu, both of them are independent non-executive directors and Mr Liu Jin James is an non-executive director.

PURCHASE, SALE OR REDEMPTION OF SECURITIES

During the Reporting Period, neither the Company nor any of its subsidiaries had purchased, sold or redeemed any of the listed securities of the Company.

COMPLIANCE WITH BOARD PRACTICE AND PROCEDURES

The Board of Directors confirmed that for the six months ended 30 June 2004, the Company had complied with the Code of Best Practice (the "Code") as set out in Appendix 14 of the Listing Rules.

On behalf of the Board
KO Sai Ying, Thomas
Chairman

Hong Kong, 16 August 2004

The directors of the Company as at the date of this report are Mr. Ko Sai Ying, Thomas, Mr. Au Yeung Ping Yuen, Terence, Mr. Tao Lung, Mr. Liao Yong Guang, Mr. Shen Song Qing, Mr. Huang Jian Ming, Mr. Jin Wei, Mr. Liu Jin, James, Mr. Lui Tin Nang and Mr. Lee Kwong Yiu.