

**THE FINANCIAL REPORT OF THE COMPANY AND ITS SUBSIDIARIES (“GROUP”) FOR THE SIX MONTHS ENDED 30 JUNE 2004 HAS NOT BEEN AUDITED**
**Consolidated Balance Sheet**
*Unit: RMB*

	Group		Company	
	As at 30 June 2004	As at 31 December 2003	As at 30 June 2004	As at 31 December 2003
<b>Assets</b>				
<b>Current assets:</b>				
Cash on hand and in bank	497,287,531.93	413,986,014.30	481,788,757.50	399,368,092.85
Short-term investment	70,000,000.00	31,177,842.00	70,000,000.00	31,177,842.00
Notes receivable	52,484,617.01	40,950,704.97	52,484,617.01	40,950,704.97
Dividend receivable	—	—	—	—
Interests receivable	—	—	—	—
Accounts receivable	397,883,836.19	259,673,380.86	397,883,836.19	259,623,380.86
Other receivable	85,646,845.66	104,258,510.22	86,971,181.55	105,353,651.38
Deposits to suppliers	3,890,993.75	4,157,098.07	3,899,979.65	4,147,040.78
Inventory	255,434,213.32	250,537,957.72	248,474,511.08	244,114,271.13
Deferred and prepaid expenses	—	—	—	—
Long term investments due within one year	—	—	—	—
Other current assets	—	—	—	—
<b>Total current assets</b>	<b>1,362,628,037.86</b>	<b>1,104,741,508.14</b>	<b>1,341,502,882.98</b>	<b>1,084,734,983.97</b>
<b>Long term investment:</b>				
Long term equity investment	80,108,518.00	80,108,518.00	91,474,203.88	92,010,811.77
Long term debenture investment	75,500.00	75,500.00	75,500.00	75,500.00
<b>Total long term investment</b>	<b>80,184,018.00</b>	<b>80,184,018.00</b>	<b>91,549,703.88</b>	<b>92,086,311.77</b>
<b>Fixed assets:</b>				
Fixed assets at cost	1,360,236,595.43	1,352,596,074.87	1,357,808,261.92	1,350,370,160.86
Less: accumulated depreciation	698,972,308.01	653,386,788.34	698,167,803.53	653,008,602.18
Fixed assets - net book value	661,264,287.42	699,209,286.53	659,640,458.39	697,361,558.68
Less: provision for devalued fixed assets	—	—	—	—
Net value of fixed assets	661,264,287.42	699,209,286.53	659,640,458.39	697,361,558.68
Construction materials	10,206,048.73	10,206,048.73	10,206,048.73	10,206,048.73
Construction-in-progress	204,919,156.28	120,597,120.29	204,919,156.28	120,597,120.29
<b>Total fixed assets</b>	<b>876,389,492.43</b>	<b>830,012,455.55</b>	<b>874,765,663.40</b>	<b>828,164,727.70</b>
<b>Intangible and other assets:</b>				
Intangible assets	74,862,403.78	70,442,662.78	74,862,403.78	70,442,662.78
Long term deferred and prepaid expenses	—	—	—	—
Other assets	—	—	—	—
<b>Total intangible and other assets</b>	<b>74,862,403.78</b>	<b>70,442,662.78</b>	<b>74,862,403.78</b>	<b>70,442,662.78</b>
<b>Deferred taxation:</b>				
Debit for deferred taxation	—	—	—	—
<b>Total assets</b>	<b>2,394,063,952.07</b>	<b>2,085,380,644.47</b>	<b>2,382,680,654.04</b>	<b>2,075,428,686.22</b>

# FINANCIAL REPORT

(PREPARED UNDER PRC ACCOUNTING STANDARDS)

	Group		Company	
	As at 30 June 2004	As at 31 December 2003	As at 30 June 2004	As at 31 December 2003
<b>Liabilities and shareholders' equity</b>				
<b>Current liabilities:</b>				
Short term loans	352,802,511.51	174,156,000.00	352,802,511.51	174,156,000.00
Notes payable	132,327,936.00	92,199,948.18	132,327,936.00	92,199,948.18
Accounts payable	144,227,266.88	145,346,593.63	137,714,140.57	140,368,400.07
Deposit from customers	9,909,766.25	8,541,346.03	9,909,766.25	8,541,346.03
Accrued payroll	—	—	—	—
Welfare and benefits payable	14,718,542.50	12,789,206.44	14,718,542.50	12,789,206.44
Dividends payable	9,502,750.57	5,795,059.07	9,502,750.57	5,795,059.07
Tax payable	3,220,767.83	-19,525,415.51	3,841,923.88	-19,201,318.56
Other payments	—	—	—	—
Other payable	41,349,154.19	37,941,290.89	40,310,526.44	37,355,557.15
Accrued expenses	6,395,022.39	7,302,547.67	6,395,022.39	7,302,547.67
Long term loans due within one year	—	—	—	—
Other current liabilities	—	—	—	—
<b>Total current liabilities</b>	<b>714,453,718.12</b>	<b>464,546,576.40</b>	<b>707,523,120.11</b>	<b>459,306,746.05</b>
<b>Long term liabilities:</b>				
Long term loans	250,000,000.00	200,000,000.00	250,000,000.00	200,000,000.00
Debentures payable	—	—	—	—
Premium on debentures payables	—	—	—	—
Long term payables due after one year	3,561,500.00	3,561,500.00	3,561,500.00	3,561,500.00
<b>Total long term liabilities</b>	<b>253,561,500.00</b>	<b>203,561,500.00</b>	<b>253,561,500.00</b>	<b>203,561,500.00</b>
<b>Deferred taxation:</b>				
Credit for deferred taxation	—	—	—	—
<b>Total liabilities</b>	<b>968,015,218.12</b>	<b>668,108,076.40</b>	<b>961,084,620.11</b>	<b>662,868,246.05</b>
<b>Minority interest:</b>				
Minority interest	3,880,568.15	3,968,071.03	—	—
<b>Shareholders' equity:</b>				
Share capital	457,312,830.00	457,312,830.00	457,312,830.00	457,312,830.00
Less: Reverted investment	—	—	—	—
Net share capital	457,312,830.00	457,312,830.00	457,312,830.00	457,312,830.00
Capital reserve	558,919,077.15	558,919,077.15	558,919,077.15	558,919,077.15
Surplus reserve	159,424,924.74	159,424,924.74	159,216,915.99	159,216,915.99
including: welfare reserves	26,291,986.91	26,291,986.91	26,222,650.66	26,222,650.66
Undistributed profit	245,939,202.04	236,903,608.28	246,147,210.79	237,111,617.03
including: Dividend in cash to be distributed	—	18,292,513.20	—	18,292,513.20
Foreign currency statement translation difference	572,131.87	744,056.87	—	—
<b>Total shareholders' equity</b>	<b>1,422,168,165.80</b>	<b>1,413,304,497.04</b>	<b>1,421,596,033.93</b>	<b>1,412,560,440.17</b>
<b>Total liabilities and shareholders' equity</b>	<b>2,394,063,952.07</b>	<b>2,085,380,644.47</b>	<b>2,382,680,654.04</b>	<b>2,075,428,686.22</b>

**Profit and loss account**

Unit: RMB

Items	Group		Company	
	2004.1-6 RMB	2003.1-6 RMB	2004.1-6 RMB	2003.1-6 RMB
1. Income from principal operations	<b>802,135,952.14</b>	677,350,595.15	<b>793,136,879.49</b>	668,990,884.59
Less: Cost of sales	<b>657,599,222.75</b>	510,900,379.84	<b>650,696,394.50</b>	505,795,175.53
Sales tax and extra charges	<b>1,114,858.70</b>	2,356,973.50	<b>1,051,788.30</b>	2,285,126.42
2. Profit from principal operations	<b>143,421,870.69</b>	164,093,241.81	<b>141,388,696.69</b>	160,910,582.64
Add: Profit from other operations	<b>925,007.40</b>	611,095.85	<b>925,007.40</b>	611,095.85
Less: Selling expenses	<b>61,696,743.26</b>	56,693,044.05	<b>59,683,583.67</b>	54,468,139.69
General and administrative expenses	<b>50,508,252.83</b>	51,463,749.64	<b>49,864,425.65</b>	50,542,622.14
Financial expenses	<b>4,999,548.94</b>	4,508,822.81	<b>5,008,049.27</b>	4,524,309.01
3. Operating profit	<b>27,142,333.06</b>	52,038,721.16	<b>27,757,645.50</b>	51,986,607.65
Add: Investment income	<b>7,920,965.43</b>	350,000.00	<b>7,384,357.54</b>	309,034.50
Allowance	<b>330,057.11</b>	—	<b>330,057.11</b>	—
Non-operating income	<b>1,408,762.00</b>	1,361,551.20	<b>1,408,762.00</b>	1,361,551.20
Less: Non-operating expenses	<b>4,452,144.19</b>	3,054,848.86	<b>4,450,244.19</b>	3,054,848.86
4. Profit before taxation	<b>32,349,973.41</b>	50,695,423.50	<b>32,430,577.96</b>	50,602,344.49
Less: Income tax	<b>5,109,369.33</b>	7,322,861.37	<b>5,102,471.00</b>	7,249,420.35
Minority shareholder's loss/gain	<b>-87,502.88</b>	19,637.99	—	—
5. Profit after taxation	<b>27,328,106.96</b>	43,352,924.14	<b>27,328,106.96</b>	43,352,924.14
Add: Undistributed profit at the beginning of the period	<b>236,903,608.28</b>	232,785,155.10	<b>237,111,617.03</b>	232,993,163.85
Other transfer	—	—	—	—
6. Distributable profit	<b>264,231,715.24</b>	276,138,079.24	<b>264,439,723.99</b>	276,346,087.99
Less: Appropriation of statutory surplus reserve	—	—	—	—
Appropriation of statutory welfare reserve	—	—	—	—
7. Profit available for distribution to shareholders	<b>264,231,715.24</b>	276,138,079.24	<b>264,439,723.99</b>	276,346,087.99
Less: Appropriation of discretionary surplus reserve	—	—	—	—
General dividends payable	<b>18,292,513.20</b>	27,438,769.80	<b>18,292,513.20</b>	27,438,769.80
8. Undistributed profit at the end of the period	<b>245,939,202.04</b>	248,699,309.44	<b>246,147,210.79</b>	248,907,318.19

**Supplement Information**

1. Income from seiling/disposing departments or companies that received investment	—	—	—	—
2. Loss from natural disaster	—	—	—	—
3. Income (decrease) of the total profit due to changes of accounting policy	—	—	—	—
4. Income (decrease) of the total profit due to changes of accounting estimation	—	—	—	—
5. Loss from recombining of debts	—	—	—	—
6. Others	—	—	—	—

## Appendix to the Profit and loss Account prepared in conformity

	Return on equity (%)				Earnings per share (RMB)			
	Fully diluted		Weighted average		Fully diluted		Weighted average	
	2004	2003	2004	2003	2004	2003	2004	2003
<b>Reported Profit</b>								
Profit from principal operations	<b>10.08</b>	11.61	<b>10.05</b>	11.56	<b>0.314</b>	0.359	<b>0.314</b>	0.359
Operating profit	<b>1.91</b>	3.68	<b>1.90</b>	3.67	<b>0.059</b>	0.114	<b>0.059</b>	0.114
Profit after taxation	<b>1.92</b>	3.07	<b>1.92</b>	3.05	<b>0.060</b>	0.095	<b>0.060</b>	0.095
Profit after taxation and extraordinary items	<b>1.65</b>	3.07	<b>1.64</b>	3.05	<b>0.051</b>	0.095	<b>0.051</b>	0.095

**Cash Flow Statement**
*Unit: RMB*

Items	Group	Company
<b>1. Cash flows from operating activities:</b>		
Cash received from sales of goods or rendering of services	555,955,548.14	540,423,126.98
Refund of tax	38,291,884.28	38,291,884.28
Other cash received relating to operating activities	4,859,039.02	4,854,707.30
<b>Sub-total of cash inflows</b>	<u>599,106,471.44</u>	<u>583,569,718.56</u>
Cash paid for goods and services	457,057,928.26	444,852,989.58
Cash paid to and on behalf of employees	57,599,284.16	56,850,666.55
Taxes paid	9,297,949.58	8,692,955.77
Other cash paid relating to operating activities	70,233,279.68	69,510,274.38
<b>Sub-total of cash outflows</b>	<u>594,188,441.68</u>	<u>579,906,886.28</u>
<b>Net cash from operating activities</b>	4,918,029.76	3,662,832.28
<b>2. Cash flows from investing activities:</b>		
Cash received from return of investment	31,177,842.00	31,177,842.00
Cash received from distribution of dividends or profits	7,920,965.43	7,920,965.43
Net cash received from disposal of fixed assets, intangible assets and other long-term assets	417,100.00	417,100.00
Other cash received relating to investing activities	—	—
<b>Sub-total of cash inflow</b>	<u>39,515,907.43</u>	<u>39,515,907.43</u>
Cash paid to acquire fixed assets, intangible assets and other long-term activities	105,354,799.65	105,152,380.15
Cash paid to acquire investments	70,000,000.00	70,000,000.00
Other cash paid relating to investing activities	—	—
<b>Sub-total of cash outflow</b>	<u>175,354,799.65</u>	<u>175,152,380.15</u>
<b>Net cash from investing activities</b>	-135,838,892.22	-135,636,472.72
<b>3. Cash flows from financing activities:</b>		
Proceeds from issue of bonds and shares	—	—
Proceeds from borrowings	276,103,815.33	276,103,815.33
Other proceeds relating to financing activities	1,855,280.72	1,855,280.72
<b>Sub-total of cash inflow</b>	<u>277,959,096.05</u>	<u>277,959,096.05</u>
Cash repayment of amounts borrowed	47,457,303.82	47,457,303.82
Cash payments of distribution of dividends or profits and interest expenses	16,107,487.14	16,107,487.14
Other cash payment relating to financing activities	—	—
<b>Sub-total of cash outflows</b>	<u>63,564,790.96</u>	<u>63,564,790.96</u>
<b>Net cash from financing activities</b>	214,394,305.09	214,394,305.09
<b>4. Effect of foreign exchange rate changes on cash</b>	-171,925.00	—
<b>5. Increases in cash and cash equivalent</b>	83,301,517.63	82,420,664.65

## Supplementary information:

Items	Group	Company
<b>1. Reconciliation of net profit to cash flows from operating activities</b>		
Net profit	27,328,106.96	27,328,106.96
Add: Minority loss/gain	-87,502.88	—
Provision for bad debt or bad debt written off	—	—
Depreciation of fixed assets	47,247,603.44	46,821,285.12
Amortization of intangible assets	1,647,759.00	1,647,759.00
Losses on disposal of fixed assets, intangible assets and other long-term assets (or deduct: gains)	-940,783.61	-940,783.61
Losses on fixed assets written off	—	—
Financial expenses	4,999,548.94	5,008,049.27
Losses arising from investments (or deduct: gains)	-7,920,965.43	-7,384,357.54
Deferred tax credit (or deduct: debit)	—	—
Decrease in inventories (or deduct: increase)	-4,896,255.60	-4,360,239.95
Decrease in operating receivables (or deduct: increase)	-130,866,598.49	-131,164,836.41
Increase in operating payables (or deduct: decrease)	68,407,117.43	66,707,849.44
Net cash flows from operating activities	4,918,029.76	3,662,832.28
<b>2. Investing and financing activities that do not involve cash receipts and payments:</b>		
Conversion of debt into capital	—	—
Convertible bonds expiring within one year	—	—
Fixed assets under finance lease	—	—
<b>3. Net increase in cash and cash equivalent:</b>		
Cash at the end of the period	497,287,531.93	481,788,757.50
Less: Cash at the beginning of the period	413,986,014.30	399,368,092.85
Cash equivalent at the end of the period	—	—
Less: Cash equivalents at the beginning of the period	—	—
Net increase in cash and cash equivalent	83,301,517.63	82,420,664.65

**Statement of Provision (Consolidated)**

Unit: RMB

Items	31 Dec. 2003	Addition for current year	Reversal for current year	Transferred out	30 June 2004
<b>1. Provision for bad debt</b>	17,011,719.14	—	11,614.02	—	17,023,333.16
Including: Account Receivable	15,658,258.42	—	11,614.02	—	15,669,872.44
Other Receivable	1,353,460.72	—	—	—	1,353,460.72
<b>2. Provision for loss on short-term investment</b>	—	—	—	—	—
Including: Stock investment	—	—	—	—	—
Bond investment	—	—	—	—	—
<b>3. Provision for loss on realisation of inventories</b>	2,384,888.63	—	—	—	2,384,888.63
Including: Goods on hand	2,384,888.63	—	—	—	2,384,888.63
Raw materials	—	—	—	—	—
<b>4. Provision for impairment on long-term investment</b>	—	—	—	—	—
Including: Investment in equity	—	—	—	—	—
Investment in bonds	—	—	—	—	—
<b>5. Provision for loss of fixed assets</b>	—	—	—	—	—
Including: Plant & building	—	—	—	—	—
Equipment	—	—	—	—	—
<b>6. Provision for impairment of intangible assets</b>	—	—	—	—	—
Including: Patents	—	—	—	—	—
Proprietary technology	—	—	—	—	—
<b>7. Provision for impairment of construction</b>	—	—	—	—	—
<b>8. Provision for impairment of designated loan receivable</b>	—	—	—	—	—

**Statement of Provision (Parent Company)**

Unit: RMB

Items	31 Dec. 2003	Addition for current year	Reversal for current year	Transferred out	30 June 2004
<b>1. Provision for bad debts</b>	17,011,719.14	—	11,614.02	—	17,023,333.16
Including: Account Receivable	15,658,258.42	—	11,614.02	—	15,669,872.44
Other Receivable	1,353,460.72	—	—	—	1,353,460.72
<b>2. Provision for loss on short-term investment</b>	—	—	—	—	—
Including: Stock investment	—	—	—	—	—
Bond investment	—	—	—	—	—
<b>3. Provision for loss on realisation of inventories</b>	2,384,888.63	—	—	—	2,384,888.63
Including: Goods on hand	2,384,888.63	—	—	—	2,384,888.63
Raw materials	—	—	—	—	—
<b>4. Provision for loss on long-term investment</b>	—	—	—	—	—
Including: Long-term equity investmnet	—	—	—	—	—
Long-term debit investment	—	—	—	—	—
<b>5. Total amounts provided for impairment of fixed assets</b>	—	—	—	—	—
Including: Plant & building	—	—	—	—	—
Equipment	—	—	—	—	—
<b>6. Provision for impairment of intangible assets</b>	—	—	—	—	—
Including: Patents	—	—	—	—	—
Proprietary technology	—	—	—	—	—
<b>7. Provision for impairment of construction in progress</b>	—	—	—	—	—
<b>8. Provision for impairment of designated loan receivable</b>	—	—	—	—	—

Notes to the accounts (unless otherwise indicated, all figures are stated in RMB'000)

## NOTES TO THE ACCOUNTS

### 1. General Background

Shandong Xinhua Pharmaceutical Company Limited (the “Company”), a listed company, was established in 1993 as the result of the reorganization of Shandong Xinhua Pharmaceutical Factory. In December 1996, the Company issued its H Shares of the People’s Republic of China (“PRC”) on The Stock Exchange of Hong Kong Limited. In July 1997, the Company listed its A Shares of the PRC on Shenzhen Stock Exchange. In November 1998, the Company became a foreign investment joint stock limited company which is approved by the Ministry of Foreign Trade and Economic Cooperation of the PRC. In Sept. 2001, the Company issued 30 million ordinary A shares and offered 3 million state-owned shares after approval.

As at 30 June 2004, the registered capital of the Company was RMB 457.31 million and the capital structure of the Company is as follows:

	Number of shares outstanding	Amount	Percentage
State-owned shares	214,440	214,440	46.89%
Legal-persons shares	16,720	16,720	3.66%
General public H shares	150,000	150,000	32.80%
General public A shares	76,153	76,153	16.65%
Total	<u>457,313</u>	<u>457,313</u>	<u>100%</u>

The principle business of the Company is to develop, produce and sell bulk pharmaceuticals, preparations and other chemical products.

### 2. Basis of presentation of financial statements

2.1. The financial statements of the Company have been prepared in conformity with the Accounting Standards for Enterprises and the Accounting Regulations of Enterprises issued by the Ministry of Finance of the PRC.

2.2. The consolidated financial statements

2.2.1. The consolidated financial statements, comprising the consolidated accounts of the Company and its subsidiaries which the Company controls more than half of the issued share capital, or controls less than half of the issued share capital, but possesses of the right of management.

2.2.2. The consolidated financial statements have been prepared in accordance with the Provisional Regulation of Consolidating Financial Statement and relevant supplementary regulations. All significant transactions and balances between the Company and its subsidiaries are eliminated upon consolidation.

### 3. Principal Accounting Policies and Accounting Estimates

3.1. Accounting period

The accounting period of the Company is from 1 January to 31 December of the calendar year.

3.2. Accounting principle and basis of valuation

The financial statements have been prepared on an accrual basis and the various assets are valued at historical cost unless otherwise indicated.

3.3. Recording currency

The Company uses RMB as its recording currency.

3.4. Translation of foreign currencies

Foreign currency transactions are translated into RMB at the rates of exchange quoted by the People’s Bank of China on the first day of the month in which the transaction occurred. Foreign currency monetary assets and liabilities are translated into RMB at the rates of exchange prevailing at the balance sheet date. Exchange differences arising are included in the operating results.

3.5. Cash equivalents

Cash equivalents are short-term (usually referring to those due within three months from the purchasing date), highly liquid investment that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value.

3.6. Provision for bad debts

The confirmation of bad debts: The debts cannot be collected even with all bankruptcy estate or heritage in a foreseeable time due to the cancellation, bankruptcy, liquidation or fund shortage and shutdown of the debtors caused by serious natural calamity and other receivables that is overdue for 3 years and clearly proven by other related evidence to be unrecoverable were confirmed to be bad debts.



The calculation of bad debts: Allowance method is adopted to calculate bad debts. The provision for bad debts is determined by using aging analysis method at the end of accounting period and included in the operating results. After approval by the board of directors or general meeting of the Company, bad debts can be recorded as losses to offset the provision for bad debt after concrete valuation for those unreceivables.

The provision for bad debts is determined as follows:

<b>Aging</b>	<b>Percentage</b>
Overdue within 1 year	0.5%
Overdue within 1-2 year	20%
Overdue within 2-3 year	60%
Overdue for more than 3 years	100%

The provision for other receivables of the Company is made in accordance with the policy for the accounts receivable. For special receivables, the provision should be determined after concrete valuation of unreceivables.

### 3.7. Inventories

Inventories, comprising mainly raw materials, work-in-progress and finished goods, low value consumables and packaging materials, are stated at cost.

The cost of raw materials includes all purchase cost, transportation fee, loading and unloading fee and insurance fee, incurred in bringing the raw materials to the present location and condition. As to the self-made semi-products and finished goods, their costs include all actual expenses incurred in the manufacturing and production process.

Costs of inventories sale: The use and sale of raw materials and the sale of semi-finished goods and finished goods were calculated on a weighted average basis.

The costs of low-value consumables and packaging materials were amortised on an one-off basis upon use.

The inventories are recorded at the actual costs or net realizable value whichever is lower. The Provision for loss on realization of inventory is determined on an individual basis whenever the cost of inventory items exceeds its net realized value. When inventories are damaged, partially or fully become obsolete or their selling price falls below cost and, as a result, their costs exceed their net realizable value, then the excess of their original costs over their net realizable value is considered as a provision for loss on realization of inventories. Net realizable value is the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to conclude the sale.

### 3.8. Long-term investment

Long-term investment includes long-term equity investments and long-term debt investments.

Long-term equity investments are recorded at initial cost on acquisition. Long-term investments are recorded by using cost method where all these investments constitute less than 20% of the capitals of the invested enterprises, or as the Company has no significant influence while it holds 20% or more than 20% of the voting capital of the invested company. The equity method is applied when the Company holds 20% or more of the voting capital of the invested company, or has significant influence when it holds less than 20% of the capitals of the invested company.

The equity investment difference between the initial investment cost and the shareholder's equity of the invested company enjoyed by the Company should be amortized to the operating results on a straight-line basis for a period stipulated in the contract. If the investment period is not stipulated in the contract, the excess of the investment cost over the shareholder's equity of the invested company enjoyed by the Company should be amortized over a period of not more than 10 years. The shortfall of investment cost over the shareholder's equity of the invested company enjoyed by the Company should be amortized over a period of not less than 10 years.

The cost of long-term debt investment acquired is the total price paid on acquisition. The interest on bonds which has been accrued and therefore included in the price paid, should be accounted for separately as receivable items on an accrual basis.

The difference between the initial costs of debt investment in which incidental expenses and unpaid interest on bonds have been subtracted and the par value of bonds is regarded as premium or discount on investment in bonds. Premium or discount on investment in bonds should be amortized over the period between the acquisition date and the maturity date in which the relevant bond interest is recognized by using a straight-line method.

Impairment of long-term investments: In case the recoverable amount of any investment is lower than the carrying amount of that investment as a result of a continuing decline in market value or changes in operating conditions of the invested enterprise, and there is no hope of recovery in the foreseeable future, then the difference between recoverable amount and the long-term investment book value would be recorded as impairment of long-term investments.

## 3.9. Fixed assets and Construction in progress

### 3.9.1. Fixed assets

Fixed assets include buildings and constructions, machinery equipment, electronic apparatus and office equipment and motor vehicles. Fixed assets refer to the production and operation of the Company with useful lives of over one year, also include other main equipment with individual values of over RMB2,000 and using lives in excess of 2 years.

The fixed assets are recorded at initial cost. The costs of the fixed assets purchased or constructed by the Company include the price and relevant taxes and other expenses for operating. The fixed assets invested by the investors are recorded at their approved value.

Fixed assets (excluding those fully depreciated) are depreciated on a straight-line basis with the estimated net residual value at zero. The depreciable life and rate for different classes of fixed assets are as follows:

Type of fixed assets	Existing expected useful lives	Annual depreciable rate
Plants and building	20 years	5%
Machinery and equipment	10 years	10%
Electronic apparatus	5 years	20%
Office equipment and motor vehicles	5 years	20%

The Company makes a provision for impairment on those fixed assets that are actually impaired (e.g., because of excessive functions, longtime inefficient capacity of utilization, significantly decreased replacement value, yield of fixed assets much lower than the normal yield of fund), based on the difference between the lower realizable value and the carrying amount of the assets. A provision for impairment of the fixed assets is made in full amount where the following situations apply:

- (1) The market values of the fixed assets have declined significantly during the period and it is not expected to recover during the remaining expected useful period;
- (2) Fixed assets will not be used because of the progress in technique and being damaged;
- (3) Fixed assets will not be used because of the assets have been restructured, disposed or suspended business;
- (4) Significant adverse changes in operating environment, such as technology, marketing, economic and legal environment;
- (5) Receivable amount of fixed assets decreased significantly due to great increase in interest rate at the same time which properly result in a change of conversion rate of receivable amount of fixed assets.
- (6) There is evidence showing the devaluation of fixed assets.

### 3.9.2 Construction in progress

The cost of construction-in-progress is determined according to expenditures that incur actually. The cost of construction work undertaken by the Company itself is determined according to direct materials, direct labor and direct construction expenses; the cost of construction work undertaken by a third party is determined according to amount paid to the contractor; and the cost of equipment installation construction is determined according to the cost of equipment, installation charges and trial run expenses.

The construction of an asset is transferred to the fixed assets account on the date it reaches its usable conditions at an estimated amount based on the budget price, the amount paid to the contractor and cost of work. The asset will be depreciated from the month following that in which it is put into use. The estimated value of the asset and its accumulated depreciation is adjusted for after the actual cost is ascertained.

The Company conducts a thorough inspection of construction-in-progress at year-end and makes a provision for impairment on any difference between the lower recoverable amount and the carrying amount of construction-in-progress on the basis of different items when one or some of the following situations exist:

- (1) construction-in-progress is suspended for quite a long time and will not be resumed within 3 years;
- (2) construction-in-progress is out of date in terms of function and technology, and there is great uncertainty that it can bring economic benefit to the Company;
- (3) other situations indicate that construction-in-progress has been impaired.

3.10. Valuation and amortization of intangible assets

Intangible assets are recorded at the actual cost on acquisition. Intangible assets purchased are recorded at the amount actually paid; intangible assets contributed by an investor are recorded at an amount agreed by all the investors; and intangible assets developed by the Company itself and a legal right to which has been obtained, such as a patent, are recorded at the amount paid for registration fees and legal fees. Expenses incurred during the process of research and development such as materials, labor and others are recorded as expenses for the period in which they are incurred.

The cost of an intangible assets of the Company is, starting from the month in which it is acquired, amortized evenly over the amortization period, which is no longer than the shortest of the expected useful life, the beneficial period as specified in the contract or the useful life specified in the law, and is charged as gains or losses of the period. If the amortization period is not specified in the contract and law, the amortization period is not more than 10 years. The Company's intangible assets include land use rights, patents, non-proprietary technologies, trade marks, etc. The land use right is amortized over an assigned period of 50 years and the software use right is over a beneficial period of 5 years.

3.11. Revenue recognition

The Company's operating revenues are mainly revenues from sale of goods. Revenues are recognized when the Company has transferred to the buyer the significant risks and rewards of ownership of the goods, retains neither continuing managerial involvement to the degree usually associated with ownership nor effective control over the goods sold, has received or obtained the evidence of receipt for related revenues, and the relevant costs can be measured reliably.

3.12. Principal Taxation

3.12.1. Income tax

The Company is registered in the High-tech Industrial Development Zone of Zibo City. Pursuant to the tax policies for enterprise registered in high-tech industrial development zones approved by the State Council, the Company is subject to PRC enterprise income tax rate of 15% as at 30 June 2004.

Zibo Xinhua-Sanhe Chemical Company Limited, a subsidiary of the Company, is subject to 15% income tax and other subsidiaries are subject to 33% income tax.

3.12.2. Value added tax

The Company is subject to value added tax for its sales revenues. VAT rate for domestic sales is 17% or 13% and the rate for export sales is 0%.

VAT input for raw materials purchased can be netted off against VAT output, the tax rate being 17%.

VAT payable for the period is the amount of VAT output after deductions of VAT input.

3.12.3. City Maintenance Construction Tax and Education Additional Expenses

Urban maintenance & construction tax and educational fees are levied based on VAT payable and business tax payable at the rates of 7% and 3% respectively.

3.13. Employee's welfare and social insurance reserve

In accordance with National and Zibo Municipal Regulations on labor administration, the Company should provide a certain percentage of the total salaries of its employees as welfare and social insurance reserve. The unpaid balance is recorded in the accounts like accrued payroll. The rates of provision are as follows:

Unemployment insurance fund	2%
Pension fund	23%
Welfare	14%
Housing fund	6%
Labor union fund	2%
Industrial injury insurance	1%
Education fund	1.5%

### 3.14. Profit Appropriation

Profit after taxation is appropriated in the following order in accordance with the Articles of Association of the Company and the relevant PRC regulations:

- (1) Make up accumulated losses of prior years;
- (2) Appropriate 10% of profit after taxation to the statutory surplus reserve;
- (3) Appropriate 5% to 10% of profit after taxation to the statutory welfare reserve;
- (4) Appropriate a discretionary surplus reserve at an amount approved by the shareholders in the shareholders meetings;
- (5) Distribute dividends to the shareholders.

### 4. Subsidiaries

The following is a detailed list of the holding subsidiaries and associates of the Company:

Company Name	Registered Capital	Amount	Ratio	Main operations	Consolidated or not
1. Zibo Xinhua Pharmacy Chain Company Limited	RMB2,000,000	RMB1,760,000	88%	Retail of pharmaceutical	Y
2. Zibo Xinhua Sanhe Chemical & Industrial Limited	USD500,000	USD350,000	70%	Research, production and sales pharmaceutical & Chemical	Y
3. Zibo Xinhua Pharmaceutical Design Institute	RMB2,000,000	RMB1,800,000	90%	Pharmaceutical project design	Y
4. Dezhou Xinhua Taikang Pharm Company Limited	RMB600,000	RMB360,000	60%	Retail of pharmaceutical	Y
5. Dongying Xinhua Pharmacy Company Limited	RMB900,000	RMB477,000	53%	Retail of pharmaceutical	Y
6. Weifang Xinhua Pharmacy Company Limited	RMB300,000	RMB165,000	55%	Retail of pharmaceutical	Y
7. Shandong Xinhua Pharmaceutical (European) GmbH	1,000,000 Euro	700,000 Euro	70%	Retail of pharmaceutical	Y
8. Sino-USA Zibo Xinhua Perrigo Pharmaceutical Company Limited	USD6,000,000	USD3,000,000	50%	Making & sale of Ibuprofen materials	N

\*1 Zibo Xinhua Pharmacy Chain Company Limited was registered on July, 1999, the registered capital is contributed by the Company and Shandong Xinhua Pharmaceutical Group Co., Ltd, which hold 88% and 12% of the registered capital, respectively. The original registered capital is RMB 1,000K. On September, 2002, the registered capital is increased to RMB2,000K.

\*2 Zibo Xinhua Sanhe Chemical & Industrial Company Limited was set up on October, 2002 by the Company, Japan Kyowa Pharmaceutical Co., Ltd and Beijing Santian Chemical Tech. Co., Ltd., which hold 70%, 25% and 5% of the registered capital, respectively. The original registered capital is USD500K.

\*3 Zibo Xinhua Pharmaceutical Design Institute Co., Ltd was set up on March, 2002 by the Company and Shandong Xinhua Pharmaceutical Group Co., Ltd., which hold 90% and 10% of the registered capital, respectively. The original registered capital is RMB2,000K.

\*4 Dezhou Xinhua Pharmaceutical Company Limited was set up on August, 2001 by Zibo Xinhua Pharmacy Chain Co., Ltd. - one of the subsidiaries of the Company and Shandong Dezhou Pharmaceutical Co., Ltd., which hold 60% and 40% of the registered capital, respectively. The original registered capital is RMB600K.

\*5 Dongying Xinhua Pharmacy Company Limited was set up on March, 2002 by Zibo Xinhua Pharmacy Co., Ltd. - one of the subsidiaries of the Company and Dongying Lanjing Tech.Co., Ltd., which hold 53% and 47% of the registered capital, respectively. The original registered capital is RMB900K.

\*6 Weifang Xinhua Pharmacy Company Limited was set up on March, 2002 by Zibo Xinhua Pharmacy Co., Ltd. - one of the subsidiaries of the Company and Shandong Kangda Pharmaceutical Co., Ltd., which hold 55% and 45% of the registered capital, respectively. The original registered capital is RMB300K.

\*7 Shandong Xinhua Pharmaceutical (European) GmbH, a new subsidiary of the Company was added in the consolidation of the Company in this fiscal year, which was established on 25 Nov. 2003. It was jointly invested by the Company and Mr. LIPENG from Germany. The registered capital was Euro1 million. The Company holds 70% of the equity and Mr. LIPENG holds 30%. By the end of 31 Dec. 2003, the Company had invested Euro 500,000, and the foreign investor had invested Euro 150,000. The Company was registered in Hamburg, Germany. Euro was the recording currency.

\*8 Sino-USA Zibo Xinhua Perrigo Pharmaceutical Company Limited was established between the Company and American Perrigo International Corporation on 11 Sept. 2003. The registered capital was USD6 million. Both parties hold 50% of the total equity. This joint venture was registered in the High-tech Industrial Development Zone in Zibo, Shandong Province. The recording currency was RMB.

**5. Monetary Fund**

	2004.6.30	2003.12.31
Cash	54	46
Bank deposits	497,234	413,940
Total	<u>497,288</u>	<u>413,986</u>

**6. Short-term Investments**

	2004.6.30		2003.12.31	
	Amounts	Provision for write-down	Amounts	Provision for write-down
Equity investments	—	—	1,174	—
Other investments	70,000	—	30,004	—
Total	<u>70,000</u>	<u>—</u>	<u>31,178</u>	<u>—</u>

**7. Notes Receivable**

	2004.6.30	2003.12.31
Trade acceptance	—	—
Bank acceptance	52,485	40,951
Total	<u>52,485</u>	<u>40,951</u>

The maturity date of notes receivable will be after June 2004. There are no mortgaged, discounted or overdue bills.

**8. Accounts receivable**

The aging analysis of accounts receivable as follows:

	2004.6.30	Proportion %	Provision for bad debts	2003.12.31	Proportion %	Provision for bad debts
Within 1 year	381,465	92.24	1,229	243,464	88.43	1,217
1 year to 2 years	13,789	3.33	3,075	15,375	5.58	3,075
2 years to 3 years	14,624	3.54	7,690	12,817	4.66	7,690
Over 3 Years	3,676	0.89	3,676	3,676	1.34	3,676
Total	<u>413,554</u>	<u>100.00</u>	<u>15,670</u>	<u>275,332</u>	<u>100.00</u>	<u>15,658</u>

There was no accounts receivable due from shareholders who hold 5% or more of the Company's shares.

**9. Other receivable**

	2004.6.30	Proportion %	Provision for bad debts	2003.12.31	Proportion %	Provision for bad debts
Within 1 year	84,743	97.41	28	63,016	59.67	28
1 year to 2 years	1,216	1.40	379	21,671	20.52	379
2 years to 3 years	378	0.43	283	20,262	19.19	283
Over 3 Years	663	0.76	663	663	0.62	663
Total	<u>87,000</u>	<u>100.00</u>	<u>1,353</u>	<u>105,612</u>	<u>100.00</u>	<u>1,353</u>

**10. Accounts Prepaid**

	2004.6.30	2003.12.31
Accounts Prepaid	<u>3,891</u>	<u>4,157</u>

There are no prepaid accounts due from shareholders who hold 5% or more of the Company's voting capital.

# FINANCIAL REPORT

(PREPARED UNDER PRC ACCOUNTING STANDARDS)

## 11. Inventories

	2004.6.30	Reserve against declining in price	2003.12.31	Reserve against declining in price
Raw materials	57,040	—	31,170	—
Work in progress	58,668	—	81,794	—
Finished goods	123,871	2,385	121,842	2,385
Goods in stock	6,960	—	6,424	—
Low value articles	9,749	—	10,162	—
Special materials for Government	1,531	—	1,531	—
Total	<u>257,819</u>	<u>2,385</u>	<u>252,923</u>	<u>2,385</u>

Impairment of inventory value was provided for on the basis of the difference between the carrying value of the finished products and the market value as at 30 June 2004.

## 12. Long-term investments

### 12.1. Long-term investments include:

	2003.12.31	Impairment	Increased	Decreased	2004.6.30	Impairment
Stock investment	80,108	—	—	—	80,108	—
Securities investment	76	—	—	—	76	—
Total	<u>80,184</u>	<u>—</u>	<u>—</u>	<u>—</u>	<u>80,184</u>	<u>—</u>

### 12.2. Long-term stock investments include:

Name of Company	The period of investment	Investment amount	% of ownership held
Tianton Securities Co.	Long-term	30,000	1.23%
Pacific insurance Co.	Long-term	7,000	0.25%
Sandong Huanzhong Pharm. Co.	Long-term	1,500	6%
Jinrui Sifang Inves. Co.	50 years	3,200	6%
Communication Bank	Long-term	13,577	
Xinhua Perrigo Pharmaceutical Co., Ltd	Long-term	24,831	50%
Total		<u>80,108</u>	

## 13. Fixed assets

	Building & construction	Machinery equipment	Motor Vehicle	Apparatus	Total
At 31 December 2003	<u>380,684</u>	<u>928,128</u>	<u>23,525</u>	<u>20,259</u>	<u>1,352,596</u>
Additions	1,981	5,794	1,019	755	9,549
Include: transferred from CIP	—	—	—	—	—
Disposal	—	1,107	801	—	1,908
At 30 June 2004	<u>382,665</u>	<u>932,815</u>	<u>23,743</u>	<u>21,014</u>	<u>1,360,237</u>
Accumulated depreciation					
At 31 December 2003	<u>174,548</u>	<u>447,324</u>	<u>16,246</u>	<u>15,269</u>	<u>653,387</u>
Additions	7,542	37,507	1,248	889	47,186
Disposal	—	799	801	—	1,600
At 30 June 2004	<u>182,090</u>	<u>484,032</u>	<u>16,693</u>	<u>16,158</u>	<u>698,973</u>
Net value at					
31 December 2003	<u>206,136</u>	<u>480,804</u>	<u>7,279</u>	<u>4,990</u>	<u>699,209</u>
Net value at					
30 June 2004	<u>200,575</u>	<u>448,783</u>	<u>7,050</u>	<u>4,856</u>	<u>661,264</u>

At the end of the accounting period there is no devaluation for the fixed assets and no provision had been withdrawn.

**14. Construction in progress**

	<b>2004.6.30</b>	2003.12.31
Construction projects	<b>204,919</b>	120,597
Total	<b>204,919</b>	120,597

**14.1. Detailed list of construction projects**

	Opening balance	Addition	Include: transferred to FA	Closing balance	Capital resources	Project budget	Project progress	Expected Date of Completion
1. Caffeine Project	8,307	11,742	—	20,049	Raised fund	160,000	100%	—
2. Xinhua (West) Int'l Industrial Zone	6,543	4,773	—	11,316	Self-owned	—	—	—
3. Xinhua (East) Int'l Industrial Zone	9,459	-5	—	9,454	Self-owned	—	—	—
4. Aspirin improvement	941	272	—	1,213	Self-owned	9,000	100%	—
5. Expansion of Ibuprofen production	1,629	329	—	1,958	Self-owned	9,500	100%	—
6. Injection GMP improvement	22,278	32,379	—	54,657	Raised fund	80,000	60%	—
7. Ibuprofen auxiliary facilities	3,509	277	—	3,786	Self-owned	7,000	—	—
8. New Chemical Area sewage	13,149	6,148	—	19,297	Self-owned	20,000	—	—
9. Waterworks in East Area	4,610	1,000	—	5,610	Self-owned	—	90%	—
10. E-base Project	725	596	—	1,321	Self-owned	2,300	60%	—
11. Rotative Waterworks	776	261	—	1,037	Self-owned	—	50%	—
12. Tablets Workshop	4,921	6,655	—	11,576	Self-owned	30,000	50%	—
13. New Preparation Renovation	—	3,399	—	3,399	Self-owned	3,000	80%	—
14. Other Projects	43,750	16,496	—	60,246	—	—	—	—
Total	<u>120,597</u>	<u>84,322</u>	<u>—</u>	<u>204,919</u>				

\*1 No specially-borrowed fund is used in construction-in-progress and there are no items to be capitalized

\*2 There is no impaired construction-in-progress at year-end and no provision for impairment is thus made.

**15. Intangible assets**

Items	Land use rights	Software use rights	Non-Patented technology	Total
Cost	80,949	1,260	6,450	88,659
The original cost at 1 January 2004	65,450	773	4,220	70,443
Accumulated amortization at 1 January 2004	11,139	467	780	12,386
Addition	4,360	20	1,450	5,830
Amortization	884	125	402	1,411
Accumulated amortization at 30 June 2004	12,023	592	1,182	13,797
Charge for the year	—	—	—	—
Net value at 30 June 2004	<u>68,926</u>	<u>668</u>	<u>5,268</u>	<u>74,862</u>
The last of the year of the amortization	<u>42</u>	<u>3</u>	<u>5</u>	<u>—</u>

At the end of the period there is no devaluation for Intangible assets and no provision had been withdrawn.

**16. Short term loans**

	<b>2004.6.30</b>	2003.12.31	<b>Monthly interest</b>
Guaranteed loans	—	—	—
Trusted loans	<b>352,803</b>	174,156	1.33%-4.779%
Total	<b>352,803</b>	174,156	

**17. Notes payables**

	<b>2004.6.30</b>	2003.12.31
Trade notes payable	—	301
Bankers' notes payable	<b>132,328</b>	91,899
Total	<b>132,328</b>	92,200



# FINANCIAL REPORT

(PREPARED UNDER PRC ACCOUNTING STANDARDS)

## 18. Accounts payable

	<b>2004.6.30</b>	2003.12.31
Accounts payable	<u>144,227</u>	<u>145,347</u>

There was no account payable due from shareholders who hold 5% or more of the Company's shares.

## 19. Deposits from customers

	<b>2004.6.30</b>	2003.12.31
Deposits from customers	<u>9,910</u>	<u>8,541</u>

Deposits aging over 1 year that had not been carried forward were mainly balance due settled with clients.

There was no deposits from customers due from shareholders who hold 5% or more of the Company's shares.

## 20. Dividend payable

Class of Shareholders	2004.6.30	2003.12.31	Reasons
State shares	—	—	
Listed Stock A-share	3,046	—	Normal Delay
Listed Stock H-share	—	—	
Others	<u>6,457</u>	<u>5,795</u>	Normal Delay
Total	<u>9,503</u>	<u>5,795</u>	

## 21. Tax payables

	2004.6.30	2003.12.31	Taxed ratio
Income tax	1,321	-3,576	15%
VAT	202	-17,289	
Operating tax	11	113	3%-5%
Urban maintenance construction tax	99	213	7%
Additional Education Expenses	42	91	3%
IIT Payable	209	209	
Land Use Tax Payable	453	415	
Real Estate Tax Payable	<u>884</u>	<u>299</u>	1.2%
Total	<u>3,221</u>	<u>-19,525</u>	

## 22. Other payable

	<b>2004.6.30</b>	2003.12.31
Other payable	<u>41,349</u>	<u>37,941</u>

There was no other payable due from shareholders who hold 5% or more of the Company's shares.

## 23. Accrued expenses

	<b>2004.6.30</b>	2003.12.31
Directors' emoluments	2,890	5,000
Audit fees	—	1,200
Export freight & Insurance	—	1,103
Others	<u>3,505</u>	—
Total	<u>6,395</u>	<u>7,303</u>

## 24. Long-term Borrowings

Terms of Loan	2004.6.30	2003.12.31	Annual rate
Guaranteed borrowing*	<u>250,000</u>	<u>200,000</u>	3.51%

\* The guaranty is provided by Shandong Xinhua Pharmaceutical Group Co., Ltd.



<b>25. Share capital</b>				<b>2004.6.30</b>	2003.12.31
I. Unlisted shares:					
1. Founder's shares:				<b>214,440</b>	214,440
Including: State shares (unlisted)				<b>214,440</b>	214,440
Legal persons shares				—	—
2. Fund raising legal-person shares (unlisted)				<b>16,720</b>	16,720
3. Transferred and allotted shares				—	—
4. Employee shares				—	—
5. Preferred stock and others				—	—
Sub-total				<b>231,160</b>	231,160
II. Listed shares					
1. Domestically listed RMB A shares				<b>76,153</b>	76,153
2. H shares (Listed shares)				<b>150,000</b>	150,000
3. Foreign-capital shares in domestic listing				—	—
4. Others				—	—
Sub-total				<b>226,153</b>	226,153
III. Total stock				<b>457,313</b>	457,313
<b>26. Capital surplus</b>					
	2003.12.31	<b>Increased</b>	<b>Decreased</b>		<b>2004.06.30</b>
Upward revaluation of assets	60,910	—	—		<b>60,910</b>
Premium on stock	496,851	—	—		<b>496,851</b>
Receipt of donation	1,158	—	—		<b>1,158</b>
Total	<u>558,919</u>	<u>—</u>	<u>—</u>		<u><b>558,919</b></u>
<b>27. Surplus reserve</b>					
	2003.12.31	<b>Increased</b>	<b>Decreased</b>		<b>2004.06.30</b>
Statutory surplus reserve	68,337	—	—		<b>68,337</b>
Discretionary surplus reserve	64,797	—	—		<b>64,797</b>
Public welfare fund	26,291	—	—		<b>26,291</b>
Total	<u>159,425</u>	<u>—</u>	<u>—</u>		<u><b>159,425</b></u>
<b>28. Appropriation of profit</b>					
				<b>2004.6.30</b>	2003.12.31
Profit after tax				<b>27,328</b>	42,076
Add: Undistributed profit at beginning of the year				<b>236,903</b>	232,785
Profit available for the year				<b>264,231</b>	274,861
Less: Appropriation of statutory surplus reserve (10%)				—	4,208
Appropriation of statutory employees welfare reserve (5%)				—	2,103
Undistributed profit available for the year				<b>264,231</b>	268,550
Less: Appropriation of discretionary surplus reserve (10%)				—	4,208
Dividends distribution				<b>18,292</b>	27,439
Undistributed profit, at 31 December 2003				—	—
Undistributed profit, at 30 June 2004				<b>245,939</b>	236,903
<b>29. Sales and cost</b>					
		<b>Sales</b>		<b>Cost</b>	
	<b>2004.1-6</b>	2003.1-6		<b>2004.1-6</b>	2003.1-6
Bulk pharmaceuticals	<b>490,542</b>	412,085		<b>409,963</b>	322,766
Include: export sales	<b>326,679</b>	249,736		<b>273,153</b>	196,083
Preparations	<b>279,854</b>	245,709		<b>217,848</b>	171,555
Chemicals and other products	<b>31,740</b>	19,557		<b>29,788</b>	16,580
Total	<u><b>802,136</b></u>	<u>677,351</u>		<u><b>657,599</b></u>	<u>510,901</u>
<b>30. Tax and additional</b>					
		<b>Standard</b>		<b>2004.1-6</b>	2003.1-6
City Construction Tax	7% of VAT payables of this year			<b>736</b>	1,650
Education Expenses Additional	3% of VAT payables of this year			<b>316</b>	707
Operating tax	5% of design fee			<b>63</b>	—
Total				<u><b>1,115</b></u>	<u>2,357</u>

# FINANCIAL REPORT

(PREPARED UNDER PRC ACCOUNTING STANDARDS)

## 31. Other operating profit

	Other operating revenue RMB'000	2004.1-6 Other operating cost RMB'000	Other operating profit RMB'000	Other operating revenue RMB'000	2003.1-6 Other operating cost RMB'000	Other operating profit RMB'000
Sales of materials	9,302	9,475	-173	12,705	13,233	-528
Sales of water, power and gas	5,420	5,285	135	5,496	5,455	41
Transfer of technology	—	—	—	50	28	22
Leasing	963	—	963	1,138	62	1,076
Total	<u>15,685</u>	<u>14,760</u>	<u>925</u>	<u>19,389</u>	<u>18,778</u>	<u>611</u>

## 32. Financial expenses

	2004.1-6	2003.1-6
Interest expenses	6,827	6,722
Banking charge	839	563
Less: Interest income	2,873	2,916
Exchange loss	204	421
Others	3	-281
Total	<u>5,000</u>	<u>4,509</u>

## 33. Investment income

	2004.1-6	2003.1-6
Short-term investment income	7,921	—
Other equity investment earnings	—	350
Total	<u>7,921</u>	<u>350</u>

## 34. Non-operating income

	2004.1-6	2003.1-6
Proceeds from disposal of fixed assets	1,198	1,309
Income from penalties	9	53
Others	202	—
Total	<u>1,409</u>	<u>1,362</u>

## 35. Non-operating expenses

	2004.1-6	2003.1-6
Loss on disposal of fixed assets	308	332
Overdue payment, fines, etc.	2	1
Others	4,142	2,722
Total	<u>4,452</u>	<u>3,055</u>

## 36. Notes to the parent company

### 36.1. Accounts receivable

The aging analysis for receivables is as follows:

	2004.6.30	Ratio %	Provision for bad debt	2003.12.31	Ratio %	Provision for bad debt
Within 1 year	381,465	92.24	1,229	243,414	88.42	1,217
1 year to 2 years	13,789	3.33	3,075	15,375	5.59	3,075
2 years to 3 years	14,624	3.54	7,690	12,817	4.66	7,690
Over 3 years	3,676	0.89	3,676	3,676	1.33	3,676
Total	<u>413,554</u>	<u>100.00</u>	<u>15,670</u>	<u>275,282</u>	<u>100.00</u>	<u>15,658</u>

There was no account receivables due from shareholders who hold 5% or more of the Company's shares.

## 36.2. Other receivables

	2004.6.30	Ratio %	Provision for bad debt	2003.12.31	Ratio %	Provision for bad debt
Within 1 year	86,067	97.44	28	64,128	60.10	28
1 year to 2 years	1,216	1.38	379	21,654	20.29	379
2 years to 3 years	378	0.43	283	20,262	18.99	283
Over 3 years	663	0.75	663	663	0.62	663
Total	<u>88,324</u>	<u>100.00</u>	<u>1,353</u>	<u>106,707</u>	<u>100.00</u>	<u>1,353</u>

## 36.3. Long-term investments

	2003.12.31	Impairment	Increased	Decreased	2004.6.30	Impairment
Stock investment	92,010	—	—	—	91,474	—
Securities Investment	76	—	—	—	76	—
Total	<u>92,086</u>	<u>—</u>	<u>—</u>	<u>—</u>	<u>91,550</u>	<u>—</u>

Include: Long-term equity investments

Name of Company	The period of investment	Initial investment amount	% of ownership held
Tiantong Securities Co.	Long-term	30,000	1.23%
Pacific insurance Co.	Long-term	7,000	0.25%
Sandong Huanzhong Pharm. Co.	Long-term	1,500	6%
Jinrui Sifang Inves. Co.	50 years	3,200	6%
Communication Bank	Long-term	13,577	
Xinhua Pharm.Design Institute	Long-term	1,800	90%
Zibo Xinhua Drug Store Chain.Co.	Long-term	1,760	88%
Zibo Xinhua Sanhe Chemical Co.	Long-term	2,897	70%
Zibo Xinhua Perrigo Pharmaceutical Co. Ltd.	Long-term	24,831	50%
Shandong Xinhua Pharmaceutical (Europe) GmbH	Long-term	4,597	70%
Total		<u>91,162</u>	

## 36.4. Sales &amp; cost

	Sales		Cost	
	2004.1-6	2003.1-6	2004.1-6	2003.1-6
Bulk pharmaceuticals	490,542	412,085	409,963	322,766
Include: export sales	326,679	249,736	273,153	196,083
Preparations	279,854	245,709	217,848	171,555
Chemicals and other products	22,741	11,197	22,885	11,474
Total	<u>793,137</u>	<u>668,991</u>	<u>650,696</u>	<u>505,795</u>

## 36.5. Investment income

	2004.1-6	2003.1-6
Short-term investment income	7,921	—
Other equity investment earnings	-537	309
Total	<u>7,384</u>	<u>309</u>

## 37. Related parties transactions

37.1. The general descriptions of the related parties as at 30 June 2004 are as below:

Name of the related parties	Nature	Representative of legal person	Registration site	Registered capital	Business scope	Relationship with the Company
Shandong Xinhua Pharmaceutical Group Company Limited	Company Limited	He Duanshi	Zhangdian, Zibo	298,500	Pharmaceutical & chemical production, trade and others	Holding company
Shandong Xinhua Industry & Trade Company Limited	Joint Stock enterprises	Fu Hengqian	Zhangdi-an, Zibo	23,200	Production and sales of bulk pharmaceuticals and others	Related party and a subsidiary of the Group Company
Shandong Xinhua Zibo Packing Company Limited	Company Limited	Yu Zurong	Zhangdi-an, Zibo	15,400	Design, production and sale of packing products	Related party and a subsidiary of the Group Company
Shandong Xinhua Zibo Xincat Pharmaceutical Company Limited	Joint Venture	Tao Jingshi	Zhangdi-an, Zibo	USD 3,105K	Production and sales of the bulk pharmaceuticals	Related party and a subsidiary of the Group Company
Shandong Zibo Chemferm Pharmaceutical Company Limited	Joint Venture	Fu Hengqian	Zhangdi-an, Zibo	USD 11,388K	Production and sale of Cephalixin and Cephadrine	Related party and a subsidiary of the Group Company
Shandong Xinhua Zibo Comprehensive Service Company Limited	Company Limited	Mi Chuanhuang	Zhangdi-an, Zibo	19,301	Comprehensive services	Related party and a subsidiary of the Group Company
Shandong Xinhua Zichuan Chemical Company Limited	Company Limited	Chen Dazheng	Zichuan, Zibo	3,174	Production and sale of bulk pharmaceuticals	Related party and a subsidiary of the Group Company

37.2. The major transactions with the related parties are described as follows:

37.2.1. Sales of products and provision of energy by the Company to the related parties

	Amount Receivable	Closing balance (Payable)	Notes
Include: Shandong Xinhua Industry & Trade Company Limited	12,100	27,893	Sales of power and waste materials
Xinhua Comprehensive Service Company Limited	210	2,135	Sales of power
Xincat pharmaceutical Company Limited	1,270	5,784	Sales of power and others
Xinhua Chemferm Pharmaceutical Company Limited	1,800	471	Sales of power
Xinhua Packing Company Limited	420	(5,181)	Sales of power

37.2.2. Raw materials and packing materials supplied by the related parties to the Company

	Amount Receivable	Closing balance (Payable)	Notes
Include: Shandong Xinhua Industry & Trade Company Limited	(22,050)	27,893	Raw materials
Zichuan Chemical Company Limited	(3,180)	(250)	Raw materials
Xinhua Packing Company Limited	(9,640)	(5,181)	Packing materials

37.2.3. Purchases of lands and buildings by the Company to the related parties

	Amount Receivable	Closing balance (Payable)	Notes
Include: Shandong Xinhua Pharmaceutical Group Company Limited	(6,212)	3,340	Lands and buildings

The transactions with the related parties are all settled at market prices.

## 38. Contingent events

None

## 39. Other matters

The Board of the Company has passed a resolution in respect of the participation in a trust program promoted by Qingdao Hisyn Trust Investment Company Limited. On 20 July 2004, the Company has signed the relative documents. The amount invested in the above-mentioned trust program is RMB130,000,000 and fully paid by the Company on 28 July 2004.