

Auditors' Report

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CERTIFIED PUBLIC ACCOUNTANTS

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**TO THE MEMBERS OF
HONG KONG PHARMACEUTICAL HOLDINGS LIMITED
(Provisional Liquidators Appointed)**
(Incorporated in Bermuda with limited liability)

We have audited the financial statements on pages 13 to 60 which have been prepared in accordance with accounting principles generally accepted in Hong Kong.

RESPECTIVE RESPONSIBILITIES OF THE PROVISIONAL LIQUIDATORS AND AUDITORS

The Provisional Liquidators are responsible for the preparation of financial statements which give a true and fair view. In preparing financial statements which give a true and fair view it is fundamental that appropriate accounting policies are selected and applied consistently. As more fully explained in Note 2 to the financial statements, the Provisional Liquidators are currently appointed to the Company, and the Provisional Liquidators have been unable to obtain, and are therefore unable to provide, all the relevant information in this regard.

It is our responsibility to form an independent opinion, based on our audit, on those financial statements and to report our opinion solely to you, as a body, in accordance with Section 90 of the Bermuda Companies Act 1981, and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report.

BASIS OF OPINION

We conducted our audit in accordance with Statements of Auditing Standards issued by the Hong Kong Institute of Certified Public Accountants (“HKICPA”), except that the scope of our work was limited as explained below.

An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgments made by the Provisional Liquidators in the preparation of the financial statements, and of whether the accounting policies are appropriate to the Company’s and the Group’s circumstances, consistently applied and adequately disclosed.

We planned our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance as to whether the financial statements are free from material misstatement. However the evidence available to us was limited as set out in detail in the following paragraphs.

As more fully explained in Note 2 to the financial statements, dealing in the Company’s shares on The Stock exchange of Hong Kong Limited (“the Stock Exchange”) has been suspended since 5 August 2004. On 13 October 2004 the High Court of Hong Kong (“the High Court”) appointed Mr. Cosimo Borrelli and Mr. Kelvin Flynn as joint and several provisional liquidators (the “Provisional Liquidators”) of the Company. Subsequent to the year end, on 23 December 2004, the Provisional Liquidators, the Company and a potential investor (“the Investor”) entered into an exclusivity agreement regarding the implementation of a restructuring proposal (the “Restructuring Proposal”).

The Restructuring Proposal is subject to the approval of all relevant parties, including the regulatory authorities, creditors and shareholders. The implementation of the Restructuring Proposal is also subject to the grant of a whitewash waiver from the Executive Director of the Securities and Futures Commission under the Hong Kong Code on Takeovers and Mergers from the obligations to make a general offer for all the shares in the Company not already owned by the Investor and parties acting in concert with it.

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The Rules Governing the Listing of Securities issued by the Stock Exchange require, inter alia, that companies whose shares are listed on the Stock Exchange submit audited financial statements to shareholders within 4 months of the balance sheet date. However, the audit of the final results of the Company and its subsidiaries for the year ended 31 March 2004 was necessarily delayed while the Restructuring Proposal was being finalised.

We were appointed auditors on 16 February 2005 which was subsequent to the end of the Company's financial year. The Provisional Liquidators were appointed on 13 October 2004 pursuant to an Order of the High Court. Upon the appointment of the Provisional Liquidators, the powers of the directors were suspended with regard to the affairs and business of the Company. As further set out in Note 2 to the financial statements, the Provisional Liquidators have not been able to provide us with all the information that we required in relation to our audit for the year ended 31 March 2004. In consequence, we were unable to carry out all of the auditing procedures necessary to obtain adequate assurance regarding the assets, liabilities, income and expenses appearing in the financial statements. There were no satisfactory audit procedures that we could adopt to obtain sufficient evidence regarding the accuracy and completeness of the assets, liabilities, income and expenses of the Company and the Group.

Since we were only appointed auditors on 16 February 2005, which was subsequent to the end of the Company's financial year, we were unable to carry out auditing procedures necessary to obtain adequate assurance regarding the quantities and condition of inventories, appearing in the balance sheet at 31 March 2004 at HK\$8,097,000. There were no other satisfactory audit procedures that we could adopt to obtain sufficient evidence regarding the existence and value of inventories. Any adjustment to the figure would have a consequential significant effect on the loss for the year and net liabilities at 31 March 2004.

As more fully explained in Note 21 to the financial statements, two of the Company's subsidiaries, Guizhou Ensure Chain Pharmacy Company Limited ("Ensure Chain") and Guizhou Ensure Medical Company Limited ("Ensure Medical"), were deconsolidated as of 31 March 2004 since the Provisional Liquidators considered control to have been lost on this date. The consolidated profit and loss account of the Group includes the results of the deconsolidated subsidiaries from 1 April 2003 up to 31 March 2004 based on available unaudited management accounts. The profit and loss accounts relating to the deconsolidated subsidiaries comprise turnover of HK\$ 64,557,000; cost of sales of HK\$53,504,000; other revenue of HK\$734,000; selling and distribution costs of HK\$8,338,000; administrative expenses of HK\$2,403,000; other operating expenses of HK\$1,127,000; finance costs of HK\$411,000; taxation of HK\$14,000 and minority interest of HK\$197,000. The deconsolidated assets and liabilities as at 31 March 2004 have been classified as investments in securities as per Note 35(b). We were unable to obtain sufficient information and there were no practical alternative audit procedures that we could perform to satisfy ourselves that the amounts consolidated in respect of the deconsolidated subsidiaries are fairly stated. Any adjustments to the amounts consolidated would affect the carrying amount of the investments in securities as at 31 March 2004 and the loss from the ordinary activities attributable to shareholders of the Group for the year then ended. In addition to the limitations in audit scope regarding the amounts consolidated, we have been unable to ascertain whether control of the two subsidiaries was lost on 31 March 2004. If control was lost subsequent to 31 March 2004, the consolidated balance sheet would include the subsidiaries' assets and liabilities amounts as set out in Note 35(b).

As disclosed in Note 41(g) to the financial statements one of the company's subsidiaries, Shanghai Hua Xin High Biotechnology Inc. ("Hua Xin"), was deconsolidated as of 30 November 2004 since the Provisional Liquidators considered control to have been lost on this date. The consolidated financial statements of the Group include the results of Hua Xin based on financial statements for the year ended 31 December 2003 audited by another firm of auditors in the PRC and unaudited management accounts for the 3 month period ended 31 March 2004. The consolidated amounts relating to Hua Xin comprises turnover of HK\$22,820,000; cost of sales of HK\$9,075,000; selling and distribution costs of HK\$5,175,000; administrative expenses of HK\$8,251,000; provisions for impairment of fixed assets of HK\$46,691,000; other operating expenses of HK\$625,000; finance costs of HK\$3,394,000; fixed assets of HK\$25,491,000; current assets of HK\$7,063,000; current liabilities of HK\$63,426,000 and long-term liabilities of HK\$11,336,000. We were unable to obtain sufficient information and there were no practical alternative audit procedures that we could perform to satisfy ourselves that the amounts consolidated in respect of Hua Xin are fairly stated. Any adjustments to the amounts consolidated would have a consequential significant effect on the loss for the year and net liabilities at 31 March 2004.

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FUNDAMENTAL UNCERTAINTIES RELATING TO THE BASIS OF PREPARATION OF FINANCIAL STATEMENTS AND CONTINGENT LIABILITIES

(i) Basis of preparation of financial statements

As more fully disclosed in Note 2 to the financial statements, the Provisional Liquidators were only appointed on 13 October 2004 pursuant to an Order of the High Court. The Provisional Liquidators are therefore not in a position to represent that all transactions entered into in the name of the Company and its subsidiaries during the period from 1 April 2003 to 31 March 2004 have been included in the financial statements.

The consolidated financial statements show a net deficiency of shareholders' funds of HK\$83,448,000 at 31 March 2004. As disclosed in Note 2 to the financial statements, the consolidated financial statements have been prepared on the going concern basis. In the opinion of the Provisional Liquidators, the Group and the Company would not be a going concern at the balance sheet date if the Restructuring Proposal is not successfully implemented.

If the Restructuring Proposal is not successfully implemented, adjustments might have to be made further to reduce the value of assets to their recoverable amounts, to provide for any further liabilities which might arise and to reclassify fixed assets as current assets.

(ii) Contingent liabilities

As disclosed in Note 36 to the financial statements, the Provisional Liquidators have not conducted full searches for liabilities of the Group and the Company since a formal adjudication process will be undertaken pursuant to the Restructuring Proposal. Accordingly there is a possibility that claims exist against the Group and the Company which have not been provided for or disclosed in these notes to the financial statements.

We consider that appropriate disclosures have been made in the financial statements concerning the above fundamental uncertainties, but we also consider that the uncertainties surrounding the circumstances under which the financial statements have been prepared are such that they form part of our overall disclaimer on the view given by the financial statements for the year ended 31 March 2004.

In forming our opinion, we also evaluated the overall adequacy of the presentation of information in the financial statements. We believe that our audit provides a reasonable basis for our opinion.

QUALIFIED OPINION: DISCLAIMER ON VIEW GIVEN BY FINANCIAL STATEMENTS

Because of the significance of the possible effects of the various limitations in evidence available to us, as set out in the Basis of Opinion section of our report above, we are unable to form an opinion as to whether the financial statements present fairly the state of affairs of the Company and the Group as at 31 March 2004 or of the Group's loss and cash flows for the year then ended. In all other respects, in our opinion the financial statements have been properly prepared in accordance with the Hong Kong Companies Ordinance.

As the Provisional Liquidators were not able to obtain all the information that we required in relation to our audit, we have not obtained all the information and explanations that we considered necessary for the purpose of our audit and we were unable to determine whether proper books of account have been maintained.

MOORE STEPHENS

Certified Public Accountants

Hong Kong
8 February 2006

Hong Kong Pharmaceutical Holdings Limited
Annual Report 2004