

On behalf of the Board of Directors, I am pleased to present the annual report of the Company for the year ended December 31, 2005.

## **RESULTS**

In 2005, the Group's turnover and net profit amounted to HK\$3,192.1 million and HK\$156.5 million, representing an increase of 30% and a decrease of 36% over 2004, respectively.

The Board of Directors does not recommend the payment of a final dividend for the year ended December 31, 2005.

## **BUSINESS REVIEW AND OUTLOOK**

### **Vitamin C Series**

The total output of this series for the year amounted to 28,655 tonnes, an increase of 56% over last year. Following the significant expansion of the production capacity in the PRC, price of vitamin C had been continuously under pressure. The average price of vitamin C decreased from US\$3.61 per kg at the beginning of the year to US\$2.94 per kg at the end of the year. The average price for the whole year was US\$3.24 per kg, a decrease of 24% as compared with US\$4.26 per kg in the previous year. The gross profit margin of the entire series decreased from 41.8% in the previous year to 25.6% in the current year.

In view of the existing production capacity in the PRC, it is expected that the weak price will last some time. The Group will continue to expand its customer base and strengthen the business relations with its existing customers. We will also increase the proportion of our downstream products according to market demand in order to improve profitability of this series.

### **Penicillin Series**

The total output of this series for the year amounted to 7,279 tonnes, an increase of 60% over last year. Owing to the intense market competition and the excessive production capacity, prices remained low. The average prices of penicillin industrial salt and amoxicillin for the year were US\$9.27 and US\$21.26 per kg respectively. The gross profit margin of the entire series decreased from 15.9% in the previous year to 6.9% in the current year.

Market consolidation still persists. However, the gradual increase in the utilization rate of the Group's production lines in Inner Mongolia will help improve the performance of this series.

### **Cephalosporin Series**

The total output of this series for the year amounted to 1,438 tonnes, an increase of 66% over last year. Demand for 7-ACA was strong in the current year and the price went up correspondingly. The average price of 7-ACA for the year was US\$92.82 per kg, an increase of 9% as compared with US\$85.13 per kg in the previous year. The gross profit margin of the entire series increased from 17.8% in the previous year to 24.4% in the current year.

Since the production capacity of 7-ACA in the PRC has increased significantly in the current year, excessive supply starts to develop. It is expected that product prices will be increasingly under pressure. At the beginning of 2006, the price of 7-ACA has declined to approximately US\$83 per kg.

**Finished Drugs**

Despite of the fierce market competition, this business unit still recorded a growth rate of 17% in the current year. Revenue increased to HK\$1,110 million with a gross profit margin of 24.2%. While the sales revenue was increasing, distribution costs also increased substantially, thereby bringing down the operating profit of this business unit to HK\$63 million in the current year, a decrease of 7% over last year.

Market competition is expected to remain fierce. The Group will continue to implement effective sales strategies so as to strive for business growth.

**Patent Drug**

The clinical trials of the patent drug, butylphthalide, in the PRC have been finished. The drug was launched to the market in the second half of the year and market response was desirable initially. As market build-up work is still in its early stage, this business unit is not expected to contribute considerable profit in the short term.

**FINANCIAL REVIEW****Liquidity and Financial Position**

In 2005, the Group's operating activities generated a net cash inflow of HK\$186,908,000. Capital expenditure reached HK\$539,000,000, which was financed by internal resources and bank loans. At December 31, 2005, the Group's current ratio was 1.10, a slight improvement as compared with 0.95 at the end of previous year. Debtor turnover period (ratio of the total of trade receivables and bills receivable balance to sales, inclusive of value added tax for sales in the PRC) decreased to 51 days as compared with 59 days in the previous year. As affected by the unfavourable market conditions, inventory turnover period (ratio of inventories balance to cost of goods sold) increased to 110 days as compared with 91 days in the previous year.

At December 31, 2005, the Group had total borrowings of HK\$1,491,038,000 (comprising bank loans of HK\$1,435,550,000 and loans from ultimate holding company of HK\$55,488,000). The maturity profile of the total borrowings spreads over a period of four years with HK\$344,804,000 repayable within one year and HK\$1,146,234,000 between one to four years. Net gearing ratio was 41%, which was calculated on the basis of the Group's total borrowings net of bank balances and cash of HK\$475,134,000 over equity at the balance sheet date.

45% of the Group's borrowings is denominated in Hong Kong dollars and the remaining 55% in Renminbi. The Group's revenues are either in Renminbi or in US dollars. Our exposure to foreign exchange rate fluctuations is limited as the exchange rates between these currencies are relatively stable.

**Pledge of Assets**

At December 31, 2005, bank balances of HK\$2,428,000 and bills receivable of HK\$3,828,000 were pledged to banks to secure banking facilities granted to the Group.

**Contingent Liabilities**

As disclosed in the Company's press announcement dated February 22, 2005, the Company and one of its subsidiary are named as, among others, defendants in certain antitrust complaints filed in the United States of America ("United States"). These antitrust complaints alleged that certain manufacturers of vitamin C in the PRC have

since at least December 2001 conspired to control prices and volume of exports of vitamin C to the United States and elsewhere in the world and that as such have been in violation of the antitrust laws in the United States. It is alleged in the antitrust complaints that the purchasers of vitamin C in the United States paid more for vitamin C than they would have paid in the absence of the alleged conspiracy and, therefore, suffered losses. The plaintiffs (purportedly as representatives of classes of similar plaintiffs) seek treble unspecified damages and other relief. Subsequent to the above-mentioned press announcement, there were some other complaints with the same nature as the above-mentioned antitrust complaints filed in the United States. Up to the date of this report, three of the antitrust complaints have been served on the Company and the subsidiary.

The directors of the Company are of the view that the allegations in the antitrust complaints are without merits and, the directors of the Company intend to contest to the claims set out in the antitrust complaints vigorously. The Group has appointed legal advisors to advise them in the legal proceedings and the outcome of the antitrust complaints cannot be estimated with certainty at this stage.

**EMPLOYEES**

At the balance sheet date, the Group had about 12,098 employees and the majority of them are employed in the PRC. The Group offers competitive remuneration packages, discretionary share options and bonuses to staff based on the performance of the Group and the individual employee.

**ACKNOWLEDGEMENT**

On behalf of the Board of Directors, I would like to take this opportunity to express our sincere thanks to our shareholders for their support and to our staff for their commitment and diligence during the year.

By order of the Board  
**CAI DONG CHEN**  
*Chairman*

Hong Kong, April 11, 2006