Management Discussion and Analysis

BUSINESS REVIEW

For the year ended 31 December 2006, the Group recorded a turnover growth of approximately 1.2% over 2005, amounting to approximately RMB841,475,000. A breakdown of the sales by product format for the year is set out as follows:

	Sales	Sales mix	Growth rate
Injections	RMB466,264,000	55.4%	2.9%
Soft Capsules	RMB248,282,000	29.5%	-4.5%
Granules	RMB111,917,000	13.3%	2.7%
Other product formats	RMB15,012,000	1.8%	61.5%

The moderate growth of turnover was primarily due to the state's initiation to strengthen administrative measures on hospitals' procurement of medicines and distribution channels. These initiations had caused hospitals to slow down purchases of medicines, leading to stagnation of cash flows in distribution channels and overall growth of the pharmaceutical industry.

For the year ended 31 December 2006, the Group posted an increase of approximately 13.0% of operating profit to approximately RMB387,034,000 as compared to last year. Net profit attributable to the equity holders of the Group for 2006 amounted to approximately RMB332,977,000, representing an increase of approximately 0.5% over the year of 2005. The moderate growth of net profit was mainly due to the overall slow down in growth of the pharmaceutical industry and the increase of our profit tax rate this year.

Injection Products

During 2006, the Group sold approximately RMB466,264,000 of injection products, representing an increase of approximately 2.9% over last year. Amongst these injection products, Qing Kai Ling injection, Shu Xie Ning injection, and Huang Qi injection recorded growth rates of approximately 7.7%, 166.0% and 1.7% in sales respectively. Nonetheless, sales of Shen Mai injection decreased by approximately 11.5% during the year. The Group believed that despite the overall slow down in growth of the pharmaceutical industry causing injection products to attain below the Group's growth target, market demand for Chinese medicine injection products remains strong. The Group will continue to focus on the business of injection products and implement strategies to strengthen the development of distribution network and points of sales to increase market coverage. During the year, a number of the Group's injection products had received the "Good Quality/Good Price" status. It is expected that Chinese medicine injection products will continue to be the product format with immense growth potential.

Injection products accounted for approximately 55.4% of the Group's total turnover for the year of 2006 as compared to 54.5% of total turnover for last year. The Group believes that it is presently the largest Chinese medicine injection manufacturer in the PRC in terms of sales volume and production capacity.

Management Discussion and Analysis

Soft Capsule Products

During 2006, the Group recorded sales of soft capsule products of approximately RMB248,282,000, representing a decrease of approximately 4.5% over last year. While sales of Huo Xiang Zheng Qi soft capsule had increased approximately 39.5%, sales of Wu Fu Xin Nao Qing soft capsule declined approximately 12.5% from last year, primarily due to the overall weakness in the pharmaceutical industry.

Soft Capsule products accounted for approximately 29.5% of the Group's turnover in 2006 as compared to 31.3% in last year. The Group believes that it is currently the largest Chinese medicine soft capsule manufacturer in the PRC in terms of sales volume and production capacity.

Granule Products

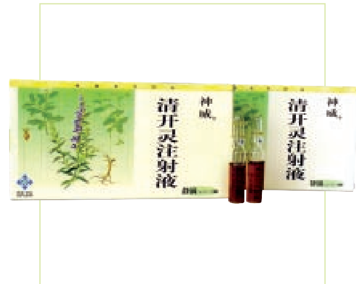
For 2006, sales of granules increased by approximately 2.7% as compared to last year, amounting to approximately RMB111,917,000. The growth can be attributable to the Group's strategies to unify the granule brand name and market positioning, strengthen marketing of the more popular granules to ensure their stable growth, despite slow growth of the pharmaceutical industry. Granule products accounted for approximately 13.3% of the Group's turnover in 2006 as compared to 13.1% in 2005.

Key Products

Shen Mai injection – for treatment of coronary heart disease, viral myocarditis and pulmonary heart disease

The amount of sales of Shen Mai injection was approximately RMB180,021,000 for 2006, representing a decline of approximately 11.5% from last year. The product accounted for approximately 21.4% of the Group's turnover. The decrease in sales of Shen Mai injection was mainly due to the administrative measure by the state authorities in the PRC on hospitals' medicine purchases during the year that led to a slow down of procurement for top selling medicines in hospitals. Shen Mai injection is a State Protected Chinese Medicine and is included in the national catalogues of medical insurance and occupational injury insurance. It is also recommended by the Ministry of Health of the PRC for treating human transmitted avian flu. The Group believes that it is the largest manufacturer and supplier of Shen Mai injection in China in terms of sales volume and enjoys competitive pricing advantage. According to an independent survey, Shen Mai injection is ranked number one in hospital purchase of Chinese medicines in the PRC. This product has enormous growth potential. The Group believes that rectification measures of the state authorities will put distribution channels more in order. The Group's Shen Mai injection is widely used in clinical applications and is very popular among medical institutions and practitioners. Leveraging on strong and established brand name, and effective implementation of pinpointed marketing strategy, the Group will continuously strive to further expand its market share and penetration in the established markets in northern and central regions of China as well as the emerging markets in the eastern and southern regions of China. The growth in sales of Shen Mai injection is accordingly expected to resume.

Qing Kai Ling injection – a widely used anti-viral medicine for treatment of viral diseases including respiratory tract infection, viral hepatitis, cerebral haemorrhage and cerebral thrombosis



Despite the overall weakness of the pharmaceutical industry, sales of Qing Kai Ling injection increased by approximately 7.7% as compared to last year amounted to approximately RMB209,610,000 for the year. It accounted for approximately 24.9% of the Group's turnover. Qing Kai Ling injection is listed in the national catalogues of medical insurance and occupational injury insurance, and is designated by the State Administration of Traditional Chinese Medicine as an indispensable Chinese medicine for the emergency wards of Chinese hospitals. It is also recommended by the Ministry of Health of the PRC for treating human transmitted avian flu. The product has broad clinical applications. As Qing Kai Ling injection is the longest in the history of the Group's manufacturing of injection products, the Group possesses strong production know-how, production cost advantage and brand equity. During the year, it was selected as a "Good Quality/Good Price" product by the state authorities. The Group believes it is the largest manufacturer of Qing Kai Ling injection in the PRC in terms of sales volume. The Group will further develop and establish alliance with strategic national distributors, improve distribution channels and strengthen marketing and promotion efforts at points of sales, to ensure the product's continuous growth.

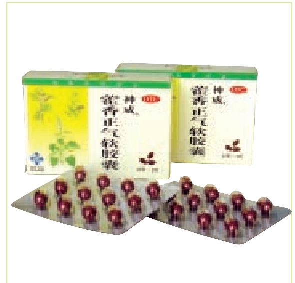
Wu Fu Xin Nao Qing soft capsule – for prevention and treatment of coronary heart disease and cerebral arteriosclerosis

As compared to last year, the sales of Wu Fu Xin Nao Qing soft capsule decreased by approximately 12.5% to RMB142,467,000 accounting for approximately 16.9% of the Group's turnover for the year. During the year, the pharmaceutical industry was affected by the administrative measures and rectification that seemingly led to stagnation of cash flows in the distribution channels. This also caused slow down in sales and distribution of the product. Wu Fu Xin Nao Qing soft capsule is one of the lowest in cost of average daily dosage among similar cardiovascular medicines and the product has been very popular. Leveraging on the strong brand name "Wu Fu", the Group will continue to strengthen its investment and support at points of sales, and increase sales promotion to turnaround the product's growth momentum.

Management Discussion and Analysis

Emerging Products

Huo Xiang Zheng Qi soft capsule – for prevention and treatment of heat stroke, stomach ache, nausea and diarrhea



For 2006, sales of Huo Xiang Zheng Qi soft capsule surged by approximately 39.5% as compared to last year, with a revenue of approximately RMB54,943,000. The product accounted for approximately 6.5% of the Group's turnover for the year. The growth for this product was mainly attributable to its brand equity, pinpointed marketing strategy, the effective implementation of first mover channel strategy and points of sales pulling strategy. The product is a State Protected Chinese Medicine and is listed in the national catalogues of medical insurance and occupational injury insurance. It is recommended by the Ministry of Health of the PRC for treating human transmitted avian flu. Huo Xiang Zheng Qi soft capsule is a very popular non-prescription product due to its effective efficacy and the high absorption rate of soft capsule. The Group will strengthen its marketing efforts and advertisement to expand market coverage. Continuous growth for this product is expected.

Shu Xie Ning injection – for treatment of cardio-cerebrovascular disease

During 2006, the amount of sales of Shu Xie Ning injection was RMB33,306,000, representing an increase of 166.0% as compared to last year. This product was put into mass production after the Group expanded its extraction capacity in early 2005. According to an independent survey, Shu Xie Ning injection, being a major type of clinical medicine for treating cardio-cerebrovascular disease, is the third most purchased Chinese medicine by hospitals in the PRC, and is also one of the State Protected Chinese Medicines. The Group believes that by leveraging the Group's advantage in production technology and economies of scale in Chinese medicine injections, this product has the potential to become a core product of the Group. With its business experience in Chinese medicine injection products and established brand name, the Group successfully introduced the product to the market during the year. This product is expected to achieve a substantial growth in the coming years.

Huang Qi injection – medicine for cardiovascular diseases and anti-viral – for treatment of viral myocarditis, heart malfunction and hepatitis

As compared to last year, sales of Huang Qi injection for 2006 increased by approximately 1.7% to approximately RMB30,336,000, accounting for approximately 3.6% of the Group's turnover for the year. The product is listed in the national catalogues of medical insurance and occupational injury insurance. With the rising trend of viral myocarditis in recent years, Huang Qi injection, with a proven efficacy on such disease, has solid foundation for future market development.

Qing Kai Ling soft capsule – for treatment of high fever, viral influenza and respiratory tract infection

Qing Kai Ling soft capsule is one of the State Protected Chinese Medicines. It is both a prescription and non-prescription medicine. It is included in the national catalogues of medical insurance and occupational injury insurance and recommended by the Ministry of Health of the PRC for treating human transmitted avian flu. Sales of Qing Kai Ling soft capsule for 2006 amounted to approximately RMB13,471,000, representing an increase of approximately 0.5% as compared to the last year. The product accounted for approximately 1.6% of the Group's turnover for the year. With strong brand name, effective implementation of channel strategy, points of sales pulling strategy and the synergy with the Qing Kai Ling injection brand, the Group expects that growth rate of this product can increase considerably.

CAPITAL EXPENDITURES

During the year, the Group completed the construction of a new logistic centre to cope with our business growth. The total costs are approximately RMB36,500,000. The Group is currently building a new injection workshop, which is scheduled to be completed in early 2008 with total cost of approximately RMB110,000,000. The new workshop is expected to double the average annual production output of injections to approximately 2 billion vials.

To enhance our research and development capability, the Group is currently establishing a new research and development center in Lang Fang, Beijing for total investment of approximately RMB33,800,000. Moreover, several other projects aiming to enhance core competence and competitive edge of the Group, including ERP implementation and remodeling of the quality inspection center are underway. Total cost for these projects is estimated to be approximately RMB25,370,000.

RESEARCH AND DEVELOPMENT

Currently, there are 28 product research projects which are either undergoing pharmaceutical and clinical trial or have completed clinical trial. Among these projects are 9 products used for treatment of various cardiovascular diseases, 3 products for treatment of digestive system illnesses and 4 products for anti-viral treatment. All of these research projects are progressed as planned.

During the year, the Ministry of Personnel of the PRC approved the Group's establishment of a post-doctoral work station, which provides the Group with enormous new strength to its research and development function. Such station further enhances the conversion of the results of research projects and provides a ground for training modern Chinese medical talents and promotion of innovation.

Management Discussion and Analysis

The Shineway brand of Qing Kai Ling injection and Jiangzhi Tongluo soft capsule were selected to be included in the "China High-Tech Products Catalogue" (the "Catalogue"). The Catalogue was jointly published by the Ministry of Science and Technology, the Ministry of Finance and the State Ministry of Taxation. The listed products must possess key knowhow in the domain of advanced technology content, proprietary knowledge, huge market potential and with economic efficiency, social efficiency and environmental efficiency. Products in the Catalogue are entitled to enjoy favorable terms, like taxation and financing, under national preferential policies.

PATENT APPLICATIONS

The Group has continuously stepped up its effort on pursuing intellectual property rights. During 2006, "a hawthorn leaf injection for treatment of cardiovascular diseases" developed by the Group was awarded the invention patent certificate by the Intellectual Property Office of the PRC. The Group kicked starting a new strategy of patent application and intellectual property rights, which strengthened the protection of the Group's new products and the related technologies under research to improve the Group's core competitive advantage in the long run. At present, the Group has obtained 3 patents for its inventions, and 12 invention patent applications are pending for approval.

STATE PROTECTED CHINESE MEDICINES

During 2006, the Group renewed the certificate of State Protected Chinese Medicines for Jian Yang Pian and Yin Zhi Huang injection and accordingly their protection periods were extended from 2006 to 2013. At present, the Group has 12 medicines under the state protected medicine scheme.

CHANGES IN REGULATIONS OF THE INDUSTRY

During 2006, the National Development and Reform Commission of the PRC (the "Commission") lowered the price caps of 67 anti-tumor western medicines, 99 anti-microbe western medicines and 32 anti-tumor Chinese medicines listed in the national insurance catalogue. On 28 February 2007, the Commission announced the adjustment of price caps on 278 Chinese medicines. Only 9 medicines of the Group are included in the announcement, including Qing Kai Ling injection, Shu Xie Ning injection, Deng Zhan Hua Su injection and Guan Xin Ning injection which contributed considerable amount of the Group turnover. But because these four injection products under the Shineway brand are labelled by the state authorities as "Good Quality/Good Price" products, the decreases of price caps for these four products are far less than those without the "Good Quality/Good Price" status. The Group believes that the decrease of price caps will not have material impact on its earnings because the average retail prices of most of its products are lower than the current price caps. The Group further believes that the "Good Quality/Good Price" status of our products represents an important competitive advantage for the Group. The policy to lower insurance price caps will accelerate closure of unsounded business, elevating market shares of larger companies and allow industry resource to flow to good companies, hence leading to the better development of our business.

In response to the occurrence of a series of incidents related to medicine safety from poor drug quality during the year, the PRC regulatory authorities resolved to rectify the supervision and management of the medicine manufacturers and promulgated a number of regulations on management of production process and product quality, which include "the Announcement of National Implementation regarding Special Inspection of Medicine Production" (《全國藥品生產專項檢查實施方案》), "The Provisional Regulations for Inspection of GMP Requirements" (《藥品GMP飛行檢查暫行規定》), "the Notice regarding Further Enhancement on the Supervision and Management of the Packing Materials for Medicines" (《關於進一步加強藥包材監督管理工作的通知》), "the Quality Management Guidelines on Production of Supplementary Materials for Medicines" (《藥用輔料生產質量管理規範》) etc. In order to strengthen the supervision and management of medicine manufacturers, the regulatory authorities intend to revoke medicine production license or GMP certificate from those manufacturers which do not comply with the requirements of the above new regulations. The Group is of the opinion that the rectification will increase public's confidence in use of medicines and facilitate healthy development of the pharmaceutical industry, though some medicine manufacturers which could not meet the regulatory standards will probably be shut down.

PROSPECT

It is expected that changes in the PRC's regulatory environment will continue in 2007. Restructuring of the medical care and pharmaceutical business framework are underway. The state authorities are determined to further intensify administrative measures on the pharmaceutical industry. A medical reform focus group consisting of members from 11 relevant ministries and commissions was formed to formulate a new framework for medical sector in the PRC. The key objectives of the reform are to position the government's forthcoming fundings and investments in public health care, and form a national system of basic medical care to enhance the welfare of all citizens in the PRC.

Medical reform in the PRC has started and it will benefit the market with sound regulations. But during the process of the reform, many might not be able to stay in the market. However, the reform can further add strength to leading enterprises and accelerate market consolidation, so large pharmaceutical companies would gain market share. With a goal to build a harmonious society, the PRC Government is determined to invest immensely in the medical sector and accelerate the development of medical care infrastructure. Under the "Rural Health Care System Formation and Development Program", being the most extensive rural health care program of the PRC has commenced. The "New Rural Cooperative Medical Insurance System" is being established to provide basic health care and medical services for all rural residents by 2010. The increased government investments in public health care and the development of community and rural medical service systems will undoubtedly increase demand for medicines, thereby laying a solid foundation for the continued growth of the pharmaceutical industry in the Eleventh Five-Year Plan period.

Management Discussion and Analysis

Despite moderate growth of the pharmaceutical industry in 2006 as impacted by the medical reform, the growth trend of the phamaceutical market in the PRC has not changed. The fast growing economy in the PRC, increase in income per capita and, rising health awareness along with aging population will certainly increase medicine consumption. Modern Chinese medicines have good efficacy and used by a large consumer base. During the Eleventh Five-Year Plan period, the PRC Government is determined to offer continuous support on the development of the Chinese medicine industry and nurture modern Chinese medicine enterprises. Hence modern Chinese medicine market will continue to growing rapidly.

GROWTH STRATEGIES

The Group will continue to implement the following established growth strategies and strives to achieve better growth and results:

1. Product mix enhancement – While increasing the revenue contribution from its core products, (namely Shen Mai, Wu Fu Xin Nao Qing and Qing Kai Ling), the Group will further nurture emerging products (including Huo Xiang, Huang Qi, Shu Xie Ning and Qing Kai Ling soft capsule) to broaden its strategic growth product portfolio.

2. Rationalization of distribution channels – The Group will foster closer strategic cooperation with cross-regional distributors which have strong distribution capabilities and strong financial position to establish a distribution network backbone and further increase the efficiency of distribution channels.

3. Strengthening support at points of sales – The Group will continue to enhance the development of a professional team to support the points of sales of prescription medicines in hospitals and OTC, as well as the "Third Point of Sale Zones" (hospitals of factories and mining fields, community clinics and rural healthcare centres) to foster the Group's brand name and demand for the Group's products.

4. Implementation of regional expansion strategies – While utilizing its advantageous position in northern, northeastern and northwestern PRC markets, the Group will also explore opportunities in southern, central and eastern PRC emerging markets which have strong demand for Chinese medicines to broaden the growth of the Group. Key strategic development regions include economically developed regions such as the Pearl River Delta, the Yangtze River Delta, Huanbo Bay costal areas, Yangtze River costal areas and cities and regions along the Beijing and Guangzhou railway.

5. The Group will continue to implement its research and development strategies with increased investments in the development of products for the treatment of chronic diseases that commonly affect the middle and old aged, anti-viral diseases and diseases that mostly affecting children.

6. The Group will continue to evaluate acquisition opportunities in a prudent manner.

Management Discussion and Analysis

FINANCIAL ANALYSIS

Turnover

In 2006, the Group continued to focus its business on Chinese medicine products and maintained stable growth in spite of the policy affects on the operational environment, recording a growth of 1.2% in total turnover as compared with last year. Turnover of injection amounted to approximately RMB466,264,000, representing an increase of around 2.9% and accounting for 55.4% of the Group's turnover. Turnover of soft capsule products amounted to approximately RMB248,282,000, representing a decrease of around 4.5% and accounting for 29.5% of the Group's turnover. Turnover of granule products amounted to approximately RMB111,917,000, representing an increase of around 2.7% and accounting for 13.3% of the Group's turnover. Turnover of the Group's product of other formats amounted approximately RMB15,012,000, accounting for 1.8% of the Group's turnover.

Turnover of the 3 key products of the Group are as follows: Shen Mai injection decreased by 11.5% from 2005 to approximately RMB180,021,000; Qing Kai Ling injection increased by 7.7% from 2005 to approximately RMB209,610,000, and Wu Fu Xin Nao Qing soft capsule decrease by about 12.5% from 2005 to approximately RMB142,467,000.

During the year, turnover of medicines for treating cardiovascular diseases, anti-viral medicines, gastroenterological medicines and medicines for treating other illness accounted for 51.8% (2005: 49.2%), 29.5% (2005: 28.0%), 6.5% (2005: 12.4%) and 12.2% (2005: 10.4%) of the Group's total turnover, respectively.

Turnover of prescription and non-prescription medicines of the Group of 2006 were approximately RMB684,122,000 and RMB157,353,000 accounting for approximately 81.3% and 18.7% of the total turnover, respectively.

As at 31 December 2006, the Group had 30 products that were included in the medical insurance catalogue.

Cost of Sales

Cost of sales of the Group in 2006 was approximately RMB249,175,000, accounting for approximately 29.6% of the total turnover. Direct materials, direct labour and other production costs accounted for approximately 74.4%, 5.0% and 20.6% of the total cost of sales.

Gross Profit Margin

During 2006, the overall gross profit margin increased from 66.9% to 70.4% as compared to last year. The average gross profit margins of injection products, soft capsule products and granule products were 77.6%, 69.4% and 45.3%, respectively. The improvement in gross profit margin is mainly attributable to the economies of scale, effective internal control, and advanced production technology to achieve high extraction rate and production yield rate. The high gross profit margin for the emerging products promoted by the Group also led to the increase in the gross profit margin of the Group during the year.

Distribution Costs

During the 2006, the overall distribution costs of the Group increased by 14.3% compared to last year, representing 21.8% (2005: 19.4%) of the Group's turnover. This was primarily attributable to the increase of distributor promotion expenses by approximately 37.9%. Distributor promotion expenses which accounted for 11.4% (2005: 8.1%) of turnover, mainly included the promotion cost subsidies to distributors. The Group had been strengthening its effort in promotion of products at sales points. While the market growth has slowed down, the Group has strengthened exploring potential markets in eastern China and southern China and has been actively participating in exhibitions, seminars and trainings, resulting in increased promotion cost subsidies to distributors and related promotion costs.

Administrative Expenses

The administrative expenses of the Group decreased by 5.2% when compared with last year, representing 8.0% (2005: 8.6%) of the Group's turnover. The decrease of the administrative expenses was mainly due to the decrease of research and development expenses by around 64.2% from last year, which in turn was primarily attributable to the slower approval procedure of the national regulatory authorities for new medicines. The research and development expenses for 2006 accounted for 0.4% (2005: 1.2%) of the Group's turnover.

Administrative expenses also comprised of non-productive depreciation expenses which accounted for 0.3% (2005: 0.2%) of the Group's turnover.

Income Tax

The PRC Enterprise Income Tax and Local Income Tax rate applicable to Shineway Pharmaceutical Co. Ltd ("Shineway Pharmaceutical") and Hebei Shineway Pharmaceutical Co. Ltd ("Hebei Shineway") is 33% of their assessable profits. Pursuant to the relevant current laws and regulations of the PRC, Shineway Pharmaceutical and Hebei Shineway are exempted from PRC Enterprise Income Tax for two years commencing from their first profitable year of operation and are entitled to a 50% relief from PRC Enterprise Income Tax for the following three years. In addition, these two companies are also exempted from Local Income Tax for five years from the first profitable year.

Pursuant to National Tax Document 1988 No. 26 (國發1988第26號), the PRC Enterprise Income Tax rate applicable to Shineway Pharmaceutical Sales Co. Ltd ("Shineway Sales") was 15% of its assessable profit.

As the year of 2006 was the third profitable year for Shineway Pharmaceutical and Hebei Shineway, the overall income tax payable for 2006 increased by about 15%. Hence, the overall effective income tax rate of the Group from 2006 to 2008 is estimated to be approximately 15%.

The Group believes that Shineway Pharmaceutical and Hebei Shineway are able to continue to enjoy 50% relief of PRC Enterprise Income Tax according to the current tax concession for high-tech enterprises of PRC, and therefore its overall effective income tax rate will most likely remain at approximately 15% after 2008.

Minority Interests

In 2005, the Group acquired the remaining 20% interests of Shineway Sales. Upon the acquisition, the Group now holds the entire interests of Shineway Sales and effectively eliminated the related minority interests.

Capital Structure

By the year ended 31 December 2006, there was no change in the capital structure and issued share capital of the Group.

Liquidity and Financial Resources

As at 31 December 2006, bank deposits of the Group approximately amounted to RMB1,582,014,000, which comprised of approximately RMB777,993,000 and HK$796,060,000 (which is equivalent to RMB804,021,000). Except for trade and operating payables, the Group did not have any other liabilities.

The Directors believe that the financial position of the Group is healthy, with sufficient financial resources to meet the requirement for future development.

Trade and Bills Receivables

As at 31 December 2006, bills receivables dropped by 52.9% as compared with 31 December 2005 since the Group encouraged customers to settle payment by cash instead of bills. Turnover days of trade and bills receivables was 1.4 days and 42.9 days (2005: 2.2 days and 70.5 days) respectively.

Inventories

Inventories balance as at 31 December 2006 increased by approximately 7.7% as compared with 31 December 2005 due to an expected increase in demand of sales in the beginning of 2007. According to inventory analysis conducted at 31 December 2006, raw materials, work in progress and finished goods accounted for approximately 35.9%, 29.9% and 34.2% (2005: 48.8%, 14.7% and 36.5%) of inventories respectively.

Finished goods inventories turnover days of 2006 were 19.0 days (2005: 13.2 days).

Property, Plant and Equipment

As at 31 December 2006, property, plant and equipment decreased by 3.0% as compared with last year.

Goodwill

Goodwill is related to the Group's acquisition of the remaining 20% ownership interests of Shineway Sales in 2005.

Management Discussion and Analysis

Trade Payables

During the period under review, turnover days of trade payables was 138.0 days (2005: 61.0 days).

Loans and Bank Borrowings

The Group did not have any loans or bank borrowings as at 31 December 2006 (2005: Nil) except for bills receivables of RMB1,368,000 (2005: Nil) and bank deposits of RMB1,882,000 (2005: Nil) were pledged to bank to secure bills payables of approximately RMB2,973,000 (2005: Nil). Accordingly, the gearing ratio based on interest bearing debt for the year is Nil (2005: Nil).

Pledge of Assets

At the time of settlement as at 31 December 2006, the Group secured the bills payables of approximately RMB2,973,000 (2005: Nil) by pledging bank deposits and bills receivables amounting approximately RMB1,882,000 (2005: Nil) and RMB1,368,000 (2005: Nil) respectively.

Contingent Liabilities

The Group did not have any contingent liabilities as at 31 December 2006 (2005: Nil).

Exposure to Fluctuations in Exchange Rates

Substantially all of the business transactions and liabilities of the Group are denominated in Renminbi and Hong Kong dollars. The Group adopts a conservative financial policy and majority of its bank deposits are in Renminbi and Hong Kong dollars. As at 31 December 2006, the Group did not have any bank liabilities, foreign exchange contracts, interest or currency swaps or other financial derivatives for hedging purpose. Therefore, the Group is not exposed to any material interest and exchange risks.

Substantial Investment and Acquisition

During 2006, the Group did not have any substantial investment and acquisition.

Employees

As at 31 December 2006, the Group has 2,155 (2005: 1,748) employees. Remuneration was determined and reviewed based on fair principles with reference to market conditions and individual performance. The Group also provided other benefits to its employees, including medical insurance and retirement benefits. The Group's employees in Hong Kong were also enrolled in the mandatory provident fund scheme.