

MANAGEMENT DISCUSSION AND ANALYSIS



BUSINESS PERFORMANCE CONDITIONS

For the year 2006, the Group recorded sales of health care products of HK\$83,690,000, representing a decrease of 16.80% from the corresponding period in the previous year, and sales of pharmaceutical products amounted to HK\$33,063,000, increasing by 9.89% from the corresponding period in the previous year, while the sales of Electronic Cigarettes Components, rose 122.86% to HK\$102,720,000 from the corresponding period in the previous year. Overall, the Group recorded a satisfactory sales turnover of HK\$219,473,000, representing an increase of 24.16% when compared with the previous year.

Since competition in the PRC's health care products and pharmaceutical products market remained intense and distribution cost, advertising and marketing expenses continued to be substantial, the business of these products was unable to generate satisfactory profit growth for the Group. Therefore, the Group has been actively developing new products with health concept such as Electronic Cigarettes Component, a tobacco substitute health care product, and satisfactory results were achieved in this area.

Meanwhile, the Group continued to seek for opportunities in the market of other non-traditional health care products for diversification, aiming to enhance our business performance and strengthen the foundation for the Group's further development.

PRODUCT DEVELOPMENT

The Group increased its investment in the development of pharmaceutical products. In 2006, the Group completed the development and proceeded to the registration of a total of 15 new pharmaceutical products. Currently, the Group has obtained the production approval of "Hai Te Ling" (咳特靈) and commenced small-scale production. Amlodipine Besylate Tablets (苯磺酸氨地平) and Pidotimod Capsule (匹多莫德膠囊) have been granted the approval for clinical research while all requisite approvals are expected to be granted in three months from the date of the Company's results announcement dated 24 April 2007. With the delay of the relevant departments of the State Pharmaceutical Administration in review and approval of the other 12 new products, it is expected that these products will all be reviewed and approved in the second half of 2007. In conclusion, the Group's profit will be enhanced with its strategy of diversification in pharmaceutical products.

REGIONAL DEVELOPMENT

In respect of the pharmaceutical business, the Group focused on establishing distribution channels and networks in 2006. The Group completed the tender in 21 provinces and cities and received the approval in pricing in 29 provinces and cities. The Group's end customers rose to 482 as compared with 252 in 2005 and this laid a solid foundation for the steady growth in sales of pharmaceutical products.

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PROSPECTS FOR THE YEAR 2007 AND DEVELOPMENT PLAN

To resume the growth track of the sales of its health care products, the Group has not only improved its products packing and increased the product mix, but also made use of direct sales channels on TV in Guangdong and Henan during the fourth quarter of 2006. In view of the delightful results achieved, the Group will expand the scale and geographical reach of tele-sales. We believe that with the above measures, the sales of health care products will resume its growth in 2007.

The Group has completed the development of certain products in 21 provinces and cities and this laid a strong foundation for its pharmaceutical products. Three products are expected to be launched in 2007 and which will enhance the stable development of the Group.

In addition, as disclosed in the announcements of the Company dated 19 March 2007 and 3 April 2007, the Group is planning to acquire the entire shareholding of Best Partners, which engages in the manufacturing and sales of Electronic Cigarettes Components. Best Partners takes an active position in developing the domestic and overseas markets under the brand name of "Ruyan" (如烟). Such plan represents an enormous development potential of the business of electronic cigarettes. Upon completion of the acquisition plan, it will greatly expand the scope of business and enhance the long term development of the Group.

LIQUIDITY AND FINANCIAL ANALYSIS

As at 31 December 2006, bank loans of the Group amounted to HK\$20.974 million, representing a decrease of HK\$15.519 million as compared to the total outstanding loans as at 31 December 2005, all of which were short-term loans due within one year and part of which were loans in Renminbi. Since movements of Renminbi against other currencies, in particular the Hong Kong dollar were more stable, the Directors do not anticipate to face any major currency exposures, therefore the Group has not arranged any currency hedge.

During the Year, an amount of HK\$1.823 million was paid as aggregate interest of bank loans (2005: HK\$2.457 million). The Group did not use property as securities for such bank facilities, nor the use of any financial instruments for hedging purposes.

Gearing ratio of the Group reduced from approximately 16.13% as at 31 December 2005 to approximately 14.67% as at 31 December 2006. This calculation is based on net borrowings of approximately HK\$44.836 million (2005: HK\$36.651 million) and shareholders fund of approximately HK\$305.686 million (2005: HK\$227.168 million).

As at 31 December 2006, the balance of the inventories amounted to HK\$131.844 million, representing an increase of HK\$44.788 million when compared with the corresponding period of the previous year.

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ACQUISITION

There were no material acquisitions and disposals of subsidiaries and associated companies during the Year. However, on 6 December 2006 the Company entered into a non-legally binding memorandum of understanding (“MOU”) with Dragon Concept Investments Limited (“Dragon Concept”), the shareholding of which is owned as to 52.11% by Mr. Wong Yen Sin and 47.89% by Mr. Hon Lik, both are executive Directors. Pursuant to the MOU, the Company shall acquire or procure to acquire not less than 30% interest in a company which shall be a direct or an indirectly subsidiary of Dragon Concept. On 13 February 2007, a sale and purchase agreement was entered into between Ability Act Investments Limited (“AAI”), the shareholding of which is owned as to 60.5% by Dragon Concept and Wealthy Well Investments Limited (“Wealthy Well”), a wholly owned subsidiary of the Company, for the acquisition of the entire issued share capital of Best Partners for a consideration of RMB1,120,000,000 (subject to adjustment) (the “Acquisition”). Details of the Acquisition are set out in the announcement of the Company dated 7 December 2006, 19 March 2007 and 3 April 2007.

CHARGE OF ASSETS

As at 31 December 2006, the Group had no bank deposits pledged to banks to secure banking facilities granted to its subsidiaries (2005: nil).

CONTINGENT LIABILITIES

As at 31 December 2006, the Group did not provide any form of guarantees for any outside companies and was not liable to any material legal proceedings of which provision for contingent liabilities was required.

EMPLOYEE POLICY

In addition to maintaining a stable employee policy, the Group will also improve employee benefits. In 2006, the Group organized enforcement, occupational quotient, manpower bottle-neck and efficient communications trainings for its management staff with an aim of upgrading their administrative abilities. Our employee policy aims at remunerating and rewarding outstanding staff while laying off staff who fail to perform satisfactorily in order to arouse the morale and initiative of the staff.