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## Important:

The board of directors ("Board") and the directors ("Directors") of Shandong Xinhua Pharmaceutical Company Limited ("Company") hereby confirm that there are no false representations, material omissions or misleading statements contained in this interim report ("Report") and they, jointly and severally, accept full responsibility for the truthfulness, accuracy and completeness of the contents of this Report. The financial report of the Company and its subsidiaries (collectively referred to as "Group") for the six months ended 30 June 2007 has not been audited.

The chairman (Ms. Guo Qin), financial controller (Mr. Zhao Songguo) and the chief of financial department (Mr. Wang Jianxin) of the Company hereby pledge that the financial report of the Company for the six months ended 30 June 2007 is true, accurate and complete.

This Report has been prepared in both Chinese and English. In the event of any discrepancy between two versions, the Chinese version shall prevail.

## COMPANY INFORMATION

Chinese Name of the Company	:	山東新華製藥股份有限公司
English Name of the Company	:	SHANDONG XINHUA PHARMACEUTICAL COMPANY LIMITED (the “Company”)
Legal Representative	:	Ms. Guo Qin
Company Secretaries	:	Mr. Cao Changqiu, Ms. Guo Lei
Telephone Number	:	86-533-2166666
Facsimile Number	:	86-533-2287508
E-mail Address of Company Secretaries	:	cqcao@xhzy.com, guolei@xhzy.com
Registered Address and Office Address	:	Chemical Industry Area of Zibo Hi-tech Industry Development Zone, Zibo City, Shandong Province, the People’s Republic of China (the “PRC”)
Postal Code	:	255005
Website of the Company	:	<a href="http://www.xhzy.com">http://www.xhzy.com</a>
E-mail Address of the Company	:	xhzy@xhzy.com
PRC newspaper for information disclosure	:	Securities Times
Website designated by the China Securities Regulatory Commission (the “CSRC”)	:	<a href="http://www.cninfo.com.cn">http://www.cninfo.com.cn</a>
Listing Information		
H Shares		
Stock Exchange	:	The Stock Exchange of Hong Kong Limited (the “SEHK”)
Abbreviated Name	:	Shandong Xinhua
Stock Code	:	0719
A Shares		
Stock Exchange	:	Shenzhen Stock Exchange (the “SZSE”)
Abbreviated Name	:	Xinhua Pharm
Stock Code	:	000756

## SUMMARY OF FINANCIAL AND OPERATING RESULTS

### 1. FINANCIAL SUMMARY PREPARED IN CONFORMITY WITH PRC ACCOUNTING STANDARDS (RMB'000)

Item	As at 30 June 2007 (Unaudited)	As at 31 December 2006 (Audited, Restated)		Change as compared to the end of last year	
		Before adjusted	After adjusted	Before adjusted	After adjusted
Total assets	2,040,490	1,880,020	1,888,203	8.54%	8.07%
Shareholders' equity	1,429,100	1,343,337	1,351,520	6.38%	5.74%
Net assets per share (RMB)	3.1250	2.9375	2.9554	6.38%	5.74%
Item	Six months ended 30 June 2007 (Unaudited)	Six months ended 30 June 2006 (Unaudited)		Change as compared to the last year	
		Before adjusted	After adjusted	Before adjusted	After adjusted
Operating profit	26,030	16,575	16,492	57.04%	57.84%
Profit before taxation	29,823	15,429	15,345	93.30%	94.34%
Profit after taxation	18,846	12,362	12,279	52.45%	53.48%
Net profit after extraordinary	14,003	10,964	10,881	27.71%	28.69%
Basic earnings per share (RMB)	0.041	0.027	0.027	51.85%	51.85%
Diluted earnings per share (RMB)	0.041	0.027	0.027	51.85%	51.85%
Return on equity (%)	1.32	0.93	0.92	an increase of 0.39 percentage point	an increase of 0.40 percentage point
Net cash flow from operating activities	78,785		6,252		1,160.14%
Net cash flow from operating activities per share (RMB)	0.172		0.014		1,128.57%

Note:

Extraordinary items include:

Items	RMB'000
Held-to-maturity investments profit/loss	1,400
Profit/loss from the disposal of non-current assets	4,035
Net amount of other non-operating income and expenses	(871)
Other extraordinary items	279
Total	<u>4,843</u>

## SUMMARY OF FINANCIAL AND OPERATING RESULTS

### 2. FINANCIAL SUMMARY PREPARED IN CONFORMITY WITH HONG KONG GENERALLY ACCEPTED ACCOUNTING PRINCIPLES (HKGAAP) (RMB'000)

#### Condensed Consolidated Income Statement

	Six months ended 30 June 2007 (Unaudited)	Six months ended 30 June 2006 (Unaudited)
Turnover	977,688	869,353
Profit before taxation	30,121	15,505
Income tax expense	(7,783)	(3,131)
Profit for the period	22,338	12,374
Include:		
Profit attributable to shareholders	19,144	12,439
Minority interests	3,194	(65)

#### Condensed Consolidated Balance Sheet

	As at 30 June 2007 (Unaudited)	As at 31 December 2006 (Audited)
Total assets	1,956,670	1,881,575
Total liabilities	(552,022)	(509,088)
Minority interests	(25,517)	(3,343)
Net assets	1,379,131	1,369,144

### 3. RECONCILIATIONS OF ACCOUNTS PREPARED IN ACCORDANCE WITH PRC ACCOUNTING STANDARDS AND HKGAAP (RMB'000)

Item	Net assets at 30 June 2007 (Unaudited)	Profit attributable to shareholders for the six months ended 30 June 2007 (Unaudited)
Prepared under PRC accounting standards	1,429,100	18,846
HKGAAP adjustments:		
Deferred taxation	(12,235)	—
Depreciation charges due to revaluation on 30 September 1996	(19,235)	(225)
Provision for education fund	12,980	523
Provision for welfare expenses	15,297	—
Surplus from revaluation for listing of H Shares	21,300	—
Change in fair value of available for sale investments	(67,892)	—
Others	(184)	—
Prepared under HKGAAP	<u>1,379,131</u>	<u>19,144</u>

## CHANGES IN SHARE CAPITAL AND SHAREHOLDERS

### 1. Share Capital structure

Unite: Share

30 Jun 2007			1 Jan 2007		
Class of shares	Number of shares (share)	% of the total share capital	Class of shares	Number of shares (share)	% of the total share capital
1. Total number of conditional tradable shares	187,820,062	41.07%	1. Total number of conditional tradable shares	204,544,593	44.73%
Stated-owned shares	163,258,735	35.70%	Stated-owned shares	163,258,735	35.70%
Domestic legal person shares	0	0%	Domestic legal person shares	16,719,500	3.66%
Conditional tradable senior management A Shares	33,727	0.01%	Conditional tradable senior management A Shares	38,758	0.01%
Others	24,527,600	5.36%	Others	24,527,600	5.36%
2. Total number of unconditional tradable shares	269,492,768	58.93%	2. Total number of unconditional tradable shares	252,768,237	55.27%
Renminbi ordinary shares (A Shares)	119,492,768	26.13%	Renminbi ordinary shares (A Shares)	102,768,237	22.47%
Overseas listed foreign shares (H shares)	150,000,000	32.80%	Overseas listed foreign shares (H Shares)	150,000,000	32.80%
3. Total number of shares	457,312,830	100.00%	3. Total number of shares	457,312,830	100.00%

Note: Domestic legal person shares were listed on 6 June, 2007 according to the share reform proposal.

## CHANGES IN SHARE CAPITAL AND SHAREHOLDERS

Tradable Schedule of Conditional Listed Tradable Shares is as follows:

No.	Name of Shareholders	Proportion of Total Share Capital	Time of Trade	Terms of Conditional Trade
1	Shandong Xinhua Pharmaceutical Group Company Limited ("SXPGC") and the shareholders of undertaking judicial auction shares (Notes 3)	5% 41.06%	G (Note 1) + 36 to 48 months G + 48 months	Note 2
2	Domestic Legal Person Shares	3.66%	Listed on 6 June, 2007	—

Note 1: Word "G" represents the first trading day (i.e. 6 June 2006) following the implementation of the revised share reform of the Company.

Note 2: SXPGC has undertaken that it shall not sell any of its A shares of the Company on the SZSE at a price less than RMB4.8 per share, (such price will be on an ex-rights basis if there is any declaration of dividends, bonus issues or capitalization of capital reserve during the period between the day of implementation of the revised share reform of the Company and sale of the shares by SXPGC) being 150% of the average of the closing prices of the listed A Shares as quoted on the SZSE in the thirty (30) trading days prior to the issuance date of the relevant notice of the shareholders' meeting. Should SXPGC breach any of the provisions of this undertaking in the sale of its shares, the proceeds resulting from such sale shall be transferred to the account of the Company and owned by the Company.

Note 3: The information of the shareholders of undertaking judicial auction shares:

Qingdao Haowei Investment Development Company Limited holds 15,000,000 shares of the Company, Zibo High-Tech Venture Capital Company Limited holds 7,632,600 shares of the Company, Huludao Bajiazi Mining Industry Company Limited holds 1,550,000 shares of the Company, Shangrao Daihu Industry Company Limited holds 345,000 shares of the Company.

- As at 30 June 2007, the Company had on record a total of 34,924 shareholders, including 60 holders of H Shares and 34,864 holders of A Shares.

## CHANGES IN SHARE CAPITAL AND SHAREHOLDERS

3. As at 30 June 2007, the ten largest shareholders of the Company were as follows:

Name of Shareholder	Types of shareholders	Number of shares held	% of the total share capital	Number of conditional tradable shares held	Number of shares being charged or freed
SXPGC	State-owned shareholder	163,258,735	35.70	163,258,735	44,680,000
HKSCC (Nominees) Limited	H shares shareholder	148,813,998	32.54	—	—
Qingdao Haowei Investment Development Company Limited	Others	15,000,000	3.28	15,000,000	15,000,000
Zibo High-Tech Venture Capital Company Limited	Others	7,632,600	1.67	7,632,600	—
Shanghai Zhengda Investment Management Company Limited	Non-State-owned Legal person	2,100,000	0.46	—	—
Huludao Bajiazi Mining Industry Company Limited	Others	1,550,000	0.34	1,550,000	—
China National Pharmaceutical Industry Corporation	Non-State-owned Legal person	1,540,000	0.34	—	—
Zibo All-purpose Service Company Limited of Shandong Xinhua Pharmaceutical Group	Non-State-owned Legal person	860,000	0.19	—	—
Liu Suying	Domestic person	759,718	0.17	—	—
Yangpu Xinyufeng Investment Company Limited	Non-State-owned Legal person	712,000	0.16	—	—

## CHANGES IN SHARE CAPITAL AND SHAREHOLDERS

4. As at 30 June 2007, the ten largest shareholders of the unconditional tradable shares of the Company were as follows:

Name of Shareholder	Number of unconditional listed shares	Class of shares
HKSCC (Nominees) Limited	148,813,998	H Shares
Shanghai Zhengda Investment Management Company Limited	2,100,000	A Shares
China National Pharmaceutical Industry Corporation	1,540,000	A Shares
Zibo All-purpose Service Company Limited of Shandong Xinhua Pharmaceutical Group	860,000	A Shares
Liu Suying	759,718	A Shares
Yangpu Xinyufeng Investment Company Limited	712,000	A Shares
Li Huaxin	602,935	A Shares
Li Fei	600,500	A Shares
China National Pharmaceutical Foreign Trade Corporation	590,000	A Shares
Shenzhen Zhonglian Guangshen Pharmaceutical (Group) Company limited	540,000	A Shares

Note: a. So far as the Directors are aware, Zibo All-purpose Service Company Limited of Shandong Xinhua Pharmaceutical Group is the wholly-owned Subsidiary of Shandong Xinhua Pharmaceutical Group Company Limited, Other than the above-mentioned claim, there is no association amongst the ten largest domestic shareholders of the Company, nor the persons acting in concert as defined in the "Rules for the Information Disclosure of Changes in the Shareholding of Listed Companies" issued by the China Securities Regulatory Commission (the "CSRC"). However, the Directors do not know whether there is any association amongst the shareholders of H Shares of the Company or persons acting in concert as referred to above.

The Directors do not know whether there is any association amongst the ten largest shareholders of unconditional tradable shares of the Company, any association between the ten largest shareholders of the Company and the ten largest shareholders of the Company or the persons acting in concert as defined in the Rules for the Information Disclosure of Changes in the Shareholding of Listed Companies issued by the CSRC.

- b. The only domestic shareholder with more than 5% of the total issued shares of the Company is SXPGC.
- c. There was no change of controlling shareholder of the Company during this reporting period.



## DIRECTORS, SUPERVISORS AND SENIOR OFFICERS

As at 30 June 2007, the number of shares held by the Directors, supervisors of the Company (“Supervisors”) and senior officers of the Company (“Senior Officers”) were as follows:

Name	Position	As at 1 January 2007 Number of Shares	Change Number of Shares	As at 30 June 2007 Number of Shares
<b>Directors:</b>				
Ms. Guo Qin	Chairman	16,852	-4,213	12,639
Mr. Liu Zhenwen	Non-executive Director	Nil		Nil
Mr. Ren Fulong	Executive Director, General Manager	Nil		Nil
Mr. Zhao Songguo	Executive Director, Deputy general manager & Financial Controller	Nil		Nil
Mr. Ma Yong	Non-executive Director	Nil		Nil
Mr. Dai Qingjun	Independent non-executive Director	Nil		Nil
Mr. Mok Chung Kwan, Stephen	Independent non-executive Director	Nil		Nil
Mr. Xu Guojun	Independent non-executive Director	Nil		Nil
Mr. Sun Minggao	Independent non-executive Director	Nil		Nil
<b>Supervisors:</b>				
Mr. Yu Gongfu	Chairman of Supervisory Committee	6,075		6,075
Mr. Gao Qinggang	Supervisor	4,370	-500 +500	4,370
Mr. Liu Qiang	Supervisor (appointed on 2 February 2007)	4,370		4,370
Mr. Zhang Yueshun	Independent Supervisor	Nil		Nil
Mr. Tao Zhichao	Independent Supervisor	Nil		Nil
Mr. Lü Zhongde	Supervisor (retired on 2 February 2007)	Nil		Nil
<b>Senior Officers:</b>				
Mr. Zhang Daiming	Deputy General Manager	Nil		Nil
Mr. Huo Yong	Deputy General Manager	4,027		4,027
Mr. Fu Hengqian	Deputy General Manager	Nil		Nil
Mr. Wang Xiaolong	Deputy General Manager	3,384		3,384
Mr. Cao Changqiu	Company Secretary	4,050	-1,012	3,038
Ms. Guo Lei	Company Secretary	Nil		Nil
<b>Total</b>		<b>43,128</b>	<b>-5,225</b>	<b>37,903</b>

All shares held by the Directors, Supervisors and Senior Officers are A Shares.

So far as the Directors, Senior Officers and Supervisors are aware, save as disclosed above, as at 30 June 2007, no Director, Senior Officer or Supervisor of the Company had any interest or short position in the shares, underlying shares and / or debentures (as the case may be) of the Company or any of its associated corporations (as defined in Part XV of the Securities and Futures Ordinance (Chapter 571 of the Laws of Hong Kong) (“SFO”)) which was required to be notified to the Company and the SEHK pursuant to Divisions 7 and 8 of Part XV of the SFO (including any interest or short position which any such Director, Senior Officer or Supervisor is taken or deemed to have under such provisions of the SFO) or which was required to be entered in the register required to be kept by the Company pursuant to Section 352 of the SFO or which was otherwise required to be notified to the Company and the SEHK pursuant to the Model Code for Securities Transactions by Directors of Listed Issuers as contained in Appendix 10 to the Rules Governing the Listing of Securities on the SEHK (the “Listing Rules”).

### CHANGES OF DIRECTORS, SUPERVISORS AND SENIOR OFFICERS

As a result of job allocation, Mr. Lü Zhongde has resigned from his position as supervisor of the Company. Pursuant to a resolution of the employee’s representatives meeting held on 2 February 2007, Mr. Liu Qiang was appointed to replace Mr. Lü Zhongde as a supervisor of the Company.

In the eighth meeting of the fifth Board of Directors held on 23 March 2007, Mr. Zhao Songguo was re-appointed as the deputy general manager and financial controller of the Company, Mr. Zhang Daiming, Mr. Fu Hengqian and Mr. Wang Xiaolong were re-appointed as the deputy general managers, Mr. Cao Changqiu and Ms. Guo Lei were re-appointed as the company secretaries.

Mr. Huo Yong has not been appointed as the deputy general manager for age reason.

Dear shareholders,

I am pleased to report the operating results of the Company for the six months ended 30 June 2007.

For the six months ended 30 June 2007, pursuant to PRC accounting standards, the operating income of the Company and its subsidiaries (collectively referred to as "the Group") was RMB968,877,000 and profit after taxation of the Company's shareholders was RMB18,846,000, representing an increase of 9.71% and an increase of 53.48% respectively, as compared to that of the same period last year.

The Group had a turnover of RMB977,688,000 and the profit attributable to shareholders of RMB19,144,000 for the six months ended 30 June 2007 under HKGAAP, representing an increase of 12.46% and an increase of 53.90% respectively, as compared with that of the same period last year.

The Board did not recommend the payment of an interim dividend for the six months ended 30 June 2007.

### REVIEW OF OPERATION

During the first half of 2007, the Group took active steps to undermine the negative impact brought by the increase in the price of the chemical raw materials, decrease in the price of pharmaceuticals and exchange rates fluctuations. The Group took advantage of the booming sale market, actively explored the domestic and overseas pharmaceutical markets and strengthened the management of the Group. As a result, the target for the first half of the year was achieved quite satisfactorily and the economic situation of the Group was improved considerably. The following is an overall review of the main businesses of the Group in the first half of 2007:

#### 1. Actively exploring the product markets

During the first half of 2007, by applying flexible and diversified marketing strategies, the Group actively participates in the market competition, and the Group had around double-digit growth in its sales of the products.

Significant results were obtained from the improvement in the marketing of the preparation products and market network was further improved. The sales of preparation products represented an increase of 25.66% as compared to that of the same period last year. The sales of bulk pharmaceuticals in the domestic market increased considerably, representing 33.05% increase as compared to that of the same period last year. During the first half of 2007, the export of SINO-USA Zibo Xinhua-Perrigo Pharmaceutical Company Limited, a subsidiary of the Company, was US\$6,920,000.

During the first half of 2007, the Group enhanced the effectiveness of the operation by controlling the operation scale and improving the product quality. The sales of the pharmaceutical products had a decrease of 20.21% as compared to that of the same period last year.

#### 2. Joint ventures and cooperation projects proceed smoothly

The allocation of resources was improved and the production of the raw materials for pharmaceuticals was enhanced. At present, the joint ventures producing raw materials are operating smoothly. Among others, the production of 3 formaldehyde has commenced and the 3 formaldehyde can be supplied to the Company for its production of the pharmaceutical products on a timely basis. The prospect of the production of salicylic acid by the joint ventures is promising. The production of enamel by co-operation has already been commenced.

By making use of the advantageous position of the Company, the cooperation between the Company and the reputable international strategic partners has been strengthened. In the first half of the year, the negotiation with the international companies on the production projects has proceeded smoothly.

#### 3. Enhancing the technology and raising profits of the Company

During the first half of 2007, the technology of the Company was improved and such improvement was expedited. The quality of the products was improved and the yield of the products increased. As a result, the Company achieved the target in relation to the improvement of technology for the production of the key products in the first half of 2007 and the consumption of raw materials decreased by RMB4,740,000 as compared to that of the same period last year.

The Company actively carried out its energy saving project and significant results were achieved. During the first half of 2007, power consumption decreased by RMB6,860,000 as compared to that of the same period last year.

#### 4. Achievement of the management

During the first half of 2007, three products of the Company obtained FDA certification of the United States and a number of the products of the Company passed the quality examinations of national, provincial and municipal authorities of the PRC.

The Company adopted public bidding in the procurement process and reduced the procurement costs. During the first half of 2007, the procurement costs of the raw materials by the Group was approximately RMB4,160,000 less than the average procurement costs in the market.

#### PLANS FOR THE SECOND HALF OF THE YEAR 2007

In relation to the second half of 2007, the situation of the pharmaceutical enterprises is not promising. There is an increase in the costs of the chemical raw materials and a decrease in rebate rates of export tax. Therefore, the enterprises will experience greater pressure in increasing its profit. Further, the PRC government has tightened the macroeconomic regulations and control which will bring about severe adverse effect on those enterprises which do not have competitive edge. However, the development of those enterprises which have competitive edge will be expedited and the production of the products will be more concentrated. Therefore, the main focus for the Group in the second half of 2007 will be as follows:

##### 1. Actively dealing with the impact brought by the change in the macro-control policy

The PRC government has implemented its macro-control policy, including changes in the monetary policy, the land policy and the adjustment in the rebate rate of export tax, and the tightening of the environmental protection policy. Further, the new GMP of the pharmaceutical industry has been launched and the new registration and management system of the pharmaceuticals has been introduced. As a result, the Group will encounter new challenges. The Group has taken or is taking practicable measures to mitigate the adverse effect brought by the macro-control policy and to expedite the development of the Group.

##### 2. Exploring the market for the products and improving the quality of the products

The Group will explore the opportunity in the market and actively develop both the domestic and international pharmaceutical markets. It will strengthen its leading position in the market of the raw materials for producing pharmaceuticals and focus on the development of the preparation product market and endeavour to increase the sales of the preparation products. The Group will carry out an in-depth study about the varieties of products, improve the quality of products and further develop the market for those products which are cost-effective and have good development potential so as to increase the profits of the Group.

The Group will continue to co-operate with the external parties and expedite the progress of cooperation projects so that the Group can achieve economic growth.

##### 3. Improving the technology further

The Group will further improve its production technology, continue to carry out the energy saving project and develop the "four first" ideology (that is, quality first, safety first, environmental protection first and energy saving first). The Group will take effective measures and devise means to develop its technology, strengthen its management, save power and energy, and reduce the consumption of raw materials so that the competitive edge of the Group can be strengthened.

By order of the Board  
**Guo Qin**  
Chairman

6 August 2007  
Zibo, Shandong, PRC

The Group is mainly engaged in the development, manufacturing and sale of bulk pharmaceuticals, pharmaceutical preparations, chemical and other products. The profit of the Group is mainly attributable to these businesses.

### 1. LIQUIDITY AND ANALYSIS OF FINANCIAL RESOURCES AND CAPITAL STRUCTURE UNDER HKGAAP

As of 30 June 2007, the liquidity ratio of the Group was 166.47%, quick ratio was 125.91%, the turnover ratio of account receivables was 350.48% (turnover ratio of account receivables = turnover / average account receivables and net value of bills x 100%) and turnover ratio of inventory was 364.14% (inventory turnover ratio = cost of sales / average net value of inventory x 100%).

There was no significant seasonal effect on the capital demand of the Group.

The main source of funds of the Group was loans from financial institutions. As at 30 June 2007, the total amount of bank loans was approximately RMB128,718,000, which were unsecured. As at 30 June 2007, cash on hand and in bank amounted to approximately RMB238,890,000 (including the pledged deposits for acceptance of bills of exchange by banks amounted to approximately RMB57,000,000).

The Group has stringent internal control systems for cash and fund management in order to strengthen financial management. The Group has sound liquidity and repayment ability.

As at 30 June 2007, the Company made a cash investment of RMB8,464,000 to purchase 20% registered capital of Shandong Zibo XinCat Pharmaceutical Company Limited, and made a cash investment of RMB5,140,000 and an equipment investment of RMB2,300,000 to Shandong Dadi Xinhua Medical Company Limited. The company is confident of the future development of the above companies.

As at 30 June 2007, the Group had income of RMB6,070,000 by disposal of some houses and land.

Apart from the above transactions, the Group did not have any significant investment, takeovers, asset acquisitions or disposals during this reporting period.

The clarification of the performance results of the Group is referred to in the section headed "Results and Financial Analysis under PRC accounting standards".

As at 30 June 2007, the number of employees of the Group amounted to 4,854. The total salaries for employees in the first half of 2007 amounted to RMB56,275,000.

As at 30 June 2007, there was no charge on the Group's assets.

There was no significant investment projects in the future plans of the Company.

The capital debt ratio of the Group was 9.33%. (capital debt ratio = total loans / share capital and total reserve x 100%)

The cash and bank balances of the Company will mainly be used as working capital for production, operation and research.

As at 30 June 2007, the Company has no contingent liabilities.

The assets and debts of the Group were mainly denominated in Renminbi. However, the Group achieved USD62,090,000 in its export for the first half of 2007. Therefore, there was a foreign exchange fluctuation risk. The Group adopted the following measures to minimize the foreign exchange fluctuation risk: 1. raising the export price in order to minimize foreign exchange fluctuation risk; and 2. when the Group enters into an export contract involving large quantities of products with other parties, the Group shall seek prior consent from the other party that both parties will bear the foreign exchange fluctuation risk should the foreign exchange fluctuation exceed the contractual limit as agreed by both parties; and 3. the Group has entered into long-term settlement agreement with financial institutions to fix exchange rates in order to mitigate foreign exchange fluctuation risks.

## 2. RESULTS AND FINANCIAL ANALYSIS UNDER PRC ACCOUNTING STANDARDS

In the first half of 2007, the Group had achieved a turnover of RMB968,877,000 from its principal business, representing an increase of 9.71% as compared to the same period last year. The increase in revenue from the principal business was mainly attributable to the fact that the Group took advantage of the booming sale market and strengthened the sale, sales of the products increased considerably. Increase in net cash and cash equivalents was RMB48,756,000, while there was a decrease of RMB121,717,000 in the same period last year. The main reason for the change was that an investment principal of RMB117,000,000 was received as the investment was mature. Operating profit amounted to RMB26,030,000, representing an increase of 57.84% as compared to the same period last year. The main reason for the increase was that the Group explored the products markets actively, increased products sales, improved the technology, reduced the consumption of raw materials and power, strengthened expenditure management and decreased sale expenses.

Total assets of the Group as at 30 June 2007 amounted to RMB2,040,490,000, representing an increase of RMB152,287,000 or 8.07% as compared to the figure of RMB1,888,203,000 as at 1 January 2007. This increase was mainly due to an increase in cash equivalents and financial assets available for sale during this reporting period. The short-term loan of the Group as at 30 June 2007 was RMB128,718,000, representing a decrease of RMB106,516,000 from RMB235,234,000 at the beginning of this year. Such decrease was attributable to the Company's adjustment of the loan structure, strengthening of the fund disbursement, a decrease in the fund costs and repayment of certain bank loans during this reporting period. Shareholders' equity (excluding minority interest) of the Company as at 30 June 2007 increased by RMB77,580,000 or 5.74%, from RMB1,351,520,000, at the beginning of this year to RMB1,429,100,000. This increase was mainly attributable to the fact that the Group had a profit of RMB18,846,000 gained from the operation and the Group had an increase of RMB67,892,000 in capital surplus resulting from the change in fair value of financial assets available for sale.

An analysis of the Group's turnover from principal operations is as follows:

By geographical location of customers	First half of 2007		First half of 2006	
	Total turnover RMB'000	Costs RMB'000	Total turnover RMB'000	Costs RMB'000
PRC (incl. Hong Kong)	516,732	436,094	516,260	427,288
Europe	139,417	114,064	127,604	106,358
Americas	150,953	126,339	164,974	143,208
Others	129,458	99,710	52,796	36,480
Total	936,560	776,207	861,634	713,334

  

By industry and By product	Income from principal operations RMB'000	Costs of sales of principal operations RMB'000	Gross profit margin (%)
Bulk pharmaceuticals	595,240	484,687	18.57
Preparations	166,903	123,067	26.26
Medical commercial logistics	172,595	167,494	2.96
Chemical products and other products	1,822	959	47.37
Total	936,560	776,207	17.12

## MANAGEMENT DISCUSSION AND ANALYSIS

An analysis of the constitution of profit as compared to 2006 is as follows:

Items	Amount (RMB'000)		% of total profit	
	Jan. – Jun. 2007	2006	Jan. – Jun. 2007	2006
Operating profit	26,030	28,126	87.28	95.97
Profit/Loss from non-operation activities	3,793	1,181	12.72	4.03
Profit before taxation	29,823	29,307	100.00	100.00

Analysis of reasons for changes: During this reporting period, the Group had an income of RMB6,070,000 by disposal of some houses and land, which resulted in profit/loss from non-operation activities having a greater proportion in profit before taxation.

### 3. USE OF PROCEEDS

On 3 September 2001, the Company raised an amount of RMB370,517,000 from the public offer and issue of 33,000,000 A Shares (including the sale of 3,000,000 State-owned shares). As at 30 June 2007, RMB320,056,000 were used in the following projects:

Name of project	Planned investment RMB'000	Actual investment Jan. - Jun. 2007 RMB'000	Accumulated amount of investment RMB'000	% of the investment	Remarks
State-level technical center renovation	74,500	—	10,123	13.59%	—
Injection GMP renovation	80,000	—	80,226	100.28%	completed
Caffeine technical renovation	160,000	—	188,201	117.63%	completed
L-350 technical renovation	29,980	—	23,442	78.19%	completed
Analgin GMP renovation	39,800	—	46,265	116.24%	completed
Total	<u>384,280</u>	<u>—</u>	<u>348,257</u>		RMB28,201,000 financed by the Company

- (1) Analgin (GMP) renovation project, L-350 technical renovation project and caffeine technical renovation were completed. Except for the fact that profit forecast of the injection GMP renovation project has yet to be realised due to the decrease in pharmaceutical prices, other projects reached their profit forecast.
- (2) The preparation stage of the renovation project of the state-level technical center was completed and construction will soon commence.

The remaining proceeds were deposited with banks and will be used in accordance with the Company's project commitments.

1. There is no material deviation between the actual corporate governance implemented by the Company and the rules and requirements of corporate governance required to be observed by listed companies in the PRC.
2. The Board did not recommend the payment of any interim dividend, nor any transfer from reserves to share capital, for the year 2007.
3. The Group was not involved in any material litigation or arbitration, whether pending or threatened during the reporting period.
4. There was no material purchase of assets or disposal of the Company's assets nor did any material mergers or acquisition involving the Company occur during this reporting period. Similarly, no transactions of such nature occurred during the last reporting period which has been carried over to this reporting period.

## 5. Material Related Party Transactions

The related party transactions of the Company are set out in Note 8 to the accounts of the Company ("Accounts") prepared in conformity with PRC accounting standards and Note 14 to the Accounts prepared in conformity with HKGAAP.

6. During this reporting period, there was no trust, subcontract and lease of the assets between the Company and other companies.
7. During this reporting period, there was no material guarantee provided by the Company, nor has any new guarantee been provided by the Company.
8. The Company and its shareholders holding more than 5% of total number of issued shares of the Company have provided undertakings for information disclosure as follows:

- (1) Within the period between the 36th to the 48th month from the listing date of the A Shares of the Company, SXPGC shall not sell any of its A shares of the Company on the SZSE at a price less than RMB4.8 per share (such price will be on an ex-rights basis if there is any declaration of dividends, bonus issues or capitalization of capital reserve during the period between the day of implementation of the revised share reform of the Company and sale of the shares by SXPGC), being 150% of the average of the closing prices of the listed A Shares as quoted on the SZSE in the thirty (30) trading days prior to the issuance date of the notice of relevant shareholders' meeting. Should SXPGC breach any of the undertakings, the proceeds resulting from such sale shall be transferred to the account of the Company and owned by the Company.
- (2) As at 1 January 2006, SXPGC owed the Company the sum of RMB9,507,000 for non-business reasons. SXPGC has repaid the capital by 30 June 2006 by way of cash. SXPGC guaranteed not to occupy any capital of the Company starting from 1 January 2007 for non-business reasons.

## 9. Purchase, Sales and Redemption of the Company's listed securities

During this reporting period, neither the Company nor its subsidiaries purchased, sold or redeemed any of its securities.

## 10. Management of Funds

During this reporting period, the Company did not appoint any person for managing the Company's funds. No such appointment was made in the preceding reporting period which has been carried over to this reporting period.

## 11. Information about holding other listed companies' equity (RMB'000)

Stock code	Abbreviated Name	Initially cost	Proportion of equity interest in investee	Book value of end of this period	Profit/loss of this period	Change of shareholder's equity of this period
601328	Bank of Communications	14,225	0.02%	82,117	0.00	67,892
Total		14,225	—	82,117	0.00	67,892



## 12. Information about holding non-listed financial enterprises and to be listed companies (RMB'000)

Name	Abbreviated Name	Number of holding	Proportion of equity interest in investee	Book value of end of this period	Profit/loss of this period	Change of shareholder's equity of this period
China Pacific Insurance (Group) Company Limited	7,000	5,000	0.07%	7,000	0	0
Total	7,000	5,000	—	7,000	0	0

## 13. Important announced information index

The announcement of “Announcement of Extraordinary General Meeting Resolutions” was published in the Hong Kong newspapers, Wen Wei Po and The Standard, on 2 January 2007, was published in the PRC domestic newspaper, Securities Times page A9, on 4 January 2007.

The announcement of “Change of Supervisor” was published in the Hong Kong newspapers, Wen Wei Po and The Standard, and in the PRC domestic newspaper, Securities Times page A3, on 5 March 2007.

The announcement of “2006 Annual Results” was published in the Hong Kong newspapers, Wen Wei Po and The Standard, the announcement of “Summary of 2006 Annual Results” was published in the PRC domestic newspaper, Securities Times page C28, on 26 March 2007.

The announcement of “The First Quarter Report of 2007” and the announcement of “The Notice of Annual General Meeting for the Year 2006” were published in the Hong Kong newspapers, Wen Wei Po and The Standard, and in the PRC domestic newspaper, Securities Times page C57, on 27 April 2007.

The announcement of “Announcement on the Listing of A Shares Subject to Selling Restrictions” was published in the Hong Kong newspapers, Wen Wei Po and The Standard, and in the PRC domestic newspaper, Securities Times page A7, on 1 June 2007.

The announcement of “Announcement of 2006 Annual General Meeting Resolutions” was published in the Hong Kong newspapers, Wen Wei Po and The Standard, and in the PRC domestic newspaper, Securities Times page C6, on 18 June 2007.

## 14. Information of reception research, communication and interview

Reception time	Reception location	Reception way	Reception objects	Main content of the discussion and the information provided
19 January 2007	Office address of the Company	Field study	Researchers of Xintai Securities Company Limited	Understand the production and operation of the Company
7 March 2007	Office address of the Company	Field study	Researchers of ABN AMRO TEDA Fund Management Company Limited	Understand the production and operation of the Company
9 March 2007	Office address of the Company	Field study	Researchers of China International Capital Corporation Limited	Understand the production, operation and development planning of the Company



**COMPLIANCE WITH THE CODE ON CORPORATE GOVERNANCE PRACTICES**

The Directors confirm that the Company has operated in compliance with the Code on Corporate Governance Practices (the “Code”) set out in Appendix 14 to the Listing Rules and has not deviated from the Code during the six months ended 30 June 2007.

**AUDIT COMMITTEE**

The Company established the Audit Committee in compliance with Rule 3.21 of the Listing Rules.

The Audit Committee along with the management have reviewed the accounting standards, principles and methods adopted by the Group, and considered matters regarding auditing, internal control and financial reporting including the unaudited interim accounts for the six months ended 30 June 2007.

The Audit Committee agreed to the accounting standards, principles and methods adopted by the Group for the unaudited interim accounts for the six months ended 30 June 2007, and it has been disclosed fully.

**INDEPENDENT NON-EXECUTIVE DIRECTOR**

The Group has complied with Rules 3.10(1) and 3.10(2) of the Listing Rules relating to appointment of a sufficient number of independent non-executive directors and at least one independent non-executive director with appropriate professional qualifications, or accounting or related financial management expertise. The Company has appointed four independent non-executive directors including one with financial management expertise, details of their biographies were set out in the 2006 Annual Report of the Company.

**MODEL CODE FOR SECURITIES TRANSACTIONS BY DIRECTORS OF LISTED ISSUERS  
 (“MODEL CODE”)**

During this reporting period, the Company has adopted a code of conduct regarding transactions by Directors on terms no less exacting than the required standards set out in the Model Code. After having made specific enquiry in this reporting period, no Director or Supervisor has infringed upon the requirements set out in the Model Code, Appendix 10 to the Listing Rules.

# FINANCIAL REPORT

(PREPARED UNDER PRC ACCOUNTING STANDARDS)

## FINANCIAL REPORT PREPARED IN CONFORMITY WITH PRC ACCOUNTING STANDARDS FOR THE SIX MONTHS ENDED 30 JUNE 2007 (UNAUDITED)

### BALANCE SHEET

Unit: RMB

Item	Notes	2007.6.30		2006.12.31	
		Consolidated	Parent company	Consolidated	Parent company
<b>Current Assets:</b>					
Cash	6.1	238,890,287.11	204,671,724.03	162,535,231.19	134,014,405.66
Trading financial assets	6.2	2,095,413.40	2,095,413.40	133,672.68	133,672.68
Notes receivable	6.3	49,203,783.36	45,448,981.76	19,430,806.25	17,461,774.68
Accounts receivable	6.4	327,322,939.19	368,296,185.90	269,249,651.02	249,187,477.63
Advances to suppliers	6.5	39,205,360.13	27,184,076.68	19,872,479.25	9,704,886.67
Interest receivable		—	—	1,548,365.00	1,548,365.00
Other receivables	6.6	41,534,717.29	52,214,695.45	41,624,438.90	53,808,365.88
Inventories	6.7	222,162,676.43	143,745,373.30	224,355,465.93	193,112,417.52
Non-current assets due within a year		—	—	—	—
Other current assets		—	—	—	—
<b>Total current assets</b>		<b>920,415,176.91</b>	<b>843,656,450.52</b>	<b>738,750,110.22</b>	<b>658,971,365.72</b>
<b>Non-current assets:</b>					
Financial assets					
available for sale	6.8	92,317,280.00	92,317,280.00	23,777,318.00	23,777,318.00
Held-to-maturity investments	6.9	75,500.00	75,500.00	117,075,500.00	117,075,500.00
Long-term receivables		—	—	—	—
Long-term equity investment	6.10	41,776,685.22	121,427,985.45	42,580,066.62	103,158,453.89
Investment property		—	—	—	—
Fixed assets	6.11	781,561,305.89	718,969,968.46	778,747,090.08	758,083,056.05
Construction in progress	6.12	99,044,304.82	98,669,153.13	81,044,943.17	81,044,943.17
Construction materials		4,763,298.61	4,763,298.61	4,877,467.51	4,877,467.51
Disposal of fixed assets		—	—	—	—
Intangible assets	6.13	92,576,838.79	91,408,305.48	93,301,452.81	93,238,519.48
Long-term prepayments		—	—	—	—
Deferred tax asset	6.14	7,959,614.80	7,615,422.95	8,049,148.23	7,615,422.95
Other non-current assets		—	—	—	—
<b>Total non-current assets</b>		<b>1,120,074,828.13</b>	<b>1,135,246,914.08</b>	<b>1,149,452,986.42</b>	<b>1,188,870,681.05</b>
<b>Total</b>		<b>2,040,490,005.04</b>	<b>1,978,903,364.60</b>	<b>1,888,203,096.64</b>	<b>1,847,842,046.77</b>

# FINANCIAL REPORT

(PREPARED UNDER PRC ACCOUNTING STANDARDS)

Unit: RMB

Item	Notes	2007.6.30		2006.12.31	
		Consolidated	Parent company	Consolidated	Parent company
<b>Current liabilities:</b>					
Short-term loans	6.15	128,718,000.00	128,718,000.00	235,233,500.00	230,233,500.00
Notes payable	6.16	178,079,279.60	178,079,279.60	97,066,900.00	97,066,900.00
Accounts payable	6.17	153,726,603.16	118,746,094.33	121,904,513.77	92,424,962.30
Advances from customers	6.18	16,002,264.09	11,277,272.30	9,650,823.43	9,118,444.86
Staff remuneration payable	6.19	26,211,944.15	26,205,779.46	31,748,340.76	31,748,340.76
Taxes payable	6.20	(4,311,541.92)	1,260,597.05	(642,994.69)	204,825.76
Interest payable		—	—	—	—
Dividends Payable	6.21	11,314,077.65	11,314,077.65	5,826,365.75	5,826,365.75
Other payables	6.22	68,109,761.89	57,504,366.64	29,021,844.06	28,392,860.89
Non-current liabilities due within a year		4,490,727.08	—	—	—
Other current liabilities		—	—	—	—
<b>Total current liabilities</b>		<b>582,341,115.70</b>	<b>533,105,467.03</b>	<b>529,809,293.08</b>	<b>495,016,200.32</b>
<b>Non-current liabilities:</b>					
Long-term borrowings		—	—	—	—
Long-term payables		—	—	—	—
Other non-current liabilities		3,561,500.00	3,561,500.00	3,561,500.00	3,561,500.00
<b>Total non-current liabilities</b>		<b>3,561,500.00</b>	<b>3,561,500.00</b>	<b>3,561,500.00</b>	<b>3,561,500.00</b>
<b>Total current liabilities</b>		<b>585,902,615.70</b>	<b>536,666,967.03</b>	<b>533,370,793.08</b>	<b>498,577,700.32</b>
<b>Shareholders' Equity:</b>					
Share capital	6.23	457,312,830.00	457,312,830.00	457,312,830.00	457,312,830.00
Capital Surplus	6.24	626,811,039.15	626,811,039.15	558,919,077.15	558,919,077.15
Less: Treasury Share		—	—	—	—
Surplus reserve	6.25	162,285,764.68	162,011,233.56	162,285,764.68	162,011,233.56
Undistributed profit	6.26	181,993,753.48	196,101,294.86	172,293,993.60	171,021,205.74
Foreign-currency statement translation difference	6.27	697,101.39	—	708,115.79	—
<b>Total equity attributable to holders of parent company</b>		<b>1,429,100,488.70</b>	<b>1,442,236,397.57</b>	<b>1,351,519,781.22</b>	<b>1,349,264,346.45</b>
Minority shareholders' equity		25,486,900.64	—	3,312,522.34	—
<b>Total shareholders' equity</b>		<b>1,454,587,389.34</b>	<b>1,442,236,397.57</b>	<b>1,354,832,303.56</b>	<b>1,349,264,346.45</b>
<b>Total liabilities and shareholders' equity</b>		<b>2,040,490,005.04</b>	<b>1,978,903,364.60</b>	<b>1,888,203,096.64</b>	<b>1,847,842,046.77</b>

# FINANCIAL REPORT

(PREPARED UNDER PRC ACCOUNTING STANDARDS)

## PROFIT AND LOSS ACCOUNT

Unit: RMB

Item	Notes	First half of 2007		First half of 2006	
		Consolidated	Parent company	Consolidated	Parent company
1. Total operating income		968,877,008.99	762,998,064.26	883,153,733.39	704,179,570.21
Include: Operating income	6.28	968,877,008.99	762,998,064.26	883,153,733.39	704,179,570.21
2. Total operating cost		947,217,544.79	731,356,083.64	869,049,250.44	689,882,159.22
Include: Operating cost	6.28	807,586,439.74	635,991,628.71	733,755,002.16	561,752,627.05
Operating tax	6.29	5,173,686.24	4,876,397.95	4,158,250.22	4,036,359.63
Selling expenses		63,606,834.91	39,546,680.95	74,963,019.33	70,684,610.87
Administrative expenses		54,374,896.95	48,296,380.09	45,776,287.37	43,261,240.17
Financial expenses	6.30	10,668,099.17	10,144,995.94	10,396,691.36	10,147,321.50
Assets impairment	6.31	5,807,587.78	(7,500,000.00)	—	—
Add: Fair value change income	6.32	1,961,740.72	1,961,740.72	—	—
Investment income	6.33	2,408,608.83	2,417,892.02	2,387,287.78	2,242,315.92
Include: Investment income of related ventures and joint ventures		604,360.96	604,360.96	(712,789.72)	(712,789.72)
3. Operating profit		26,029,813.75	36,021,613.36	16,491,770.73	16,539,726.91
Add: Non-operating income	6.34	11,066,301.45	11,046,141.45	499,338.04	499,223.80
Less: Non-operating expenses	6.35	7,273,218.05	6,887,825.76	1,645,757.92	1,644,914.89
Include: Loss from the disposal of non-current assets		(4,746,758.05)	(4,845,837.19)	(49,875.71)	(49,875.71)
4. Profit before taxation		29,822,897.15	40,179,929.05	15,345,350.85	15,394,035.82
Less: Income tax	6.36	7,783,274.15	5,953,583.33	3,130,872.75	3,110,135.23
5. Profit after taxation		22,039,623.00	34,226,345.72	12,214,478.10	12,283,900.59
Profit attributable to the equity shareholders of the Parent		18,846,016.48	34,226,345.72	12,279,060.65	12,283,900.59
Minority interest		3,193,606.52	—	(64,582.55)	—
6. Earnings per share					
1) Basic earnings per share		0.041	0.075	0.027	0.027
2) Diluted earnings per share		0.041	0.075	0.027	0.027

## STATEMENT OF CASH FLOW

Unit: RMB

Item	Notes	First half of 2007		First half of 2006	
		Consolidated	Parent company	Consolidated	Parent company
<b>1. Cash flows from operating activities:</b>					
Cash received from product sales and rendering of services		680,646,077.63	552,046,894.08	673,730,563.51	601,850,545.10
Refund of tax and levies received		10,104,546.12	5,300,001.35	11,541,682.78	11,541,682.78
Other cash received relating to operating activities	6.37	10,069,004.07	9,645,474.09	4,892,710.99	2,315,842.56
<b>Sub-total of cash inflows from operating activities</b>		<b>700,819,627.82</b>	<b>566,992,369.52</b>	<b>690,164,957.28</b>	<b>615,708,070.44</b>
Cash paid for purchase of goods and receipt of services		433,394,725.31	339,918,844.81	527,800,037.40	462,288,423.32
Cash paid to and on behalf of employees		79,462,826.33	74,488,288.69	63,641,492.23	61,898,581.28
Taxes and levies paid		29,359,197.85	24,428,518.25	24,153,792.75	23,219,354.87
Other cash paid relating to operating activities	6.38	79,817,611.87	63,892,351.26	68,317,520.02	64,442,119.03
<b>Sub-total of cash outflows from operating activities</b>		<b>622,034,361.36</b>	<b>502,728,003.01</b>	<b>683,912,842.40</b>	<b>611,848,478.50</b>
<b>Net cash flows from operating activities</b>		<b>78,785,266.46</b>	<b>64,264,366.51</b>	<b>6,252,114.88</b>	<b>3,859,591.94</b>
<b>2. Cash flows from investment activities:</b>					
Cash received from redemption of investments		117,000,000.00	117,000,000.00	—	—
Cash received from returns on investments		3,361,896.06	3,361,896.06	3,117,205.00	3,117,205.00
Net cash received from disposal of fixed assets, intangible assets and other long-term assets		3,036,996.00	3,023,300.00	702,100.00	702,100.00
Other cash received relating to investment activities		—	—	—	—
<b>Sub-total of cash inflows from investment activities</b>		<b>123,398,892.06</b>	<b>123,385,196.06</b>	<b>3,819,305.00</b>	<b>3,819,305.00</b>
Cash paid for acquisition of fixed assets, intangible assets and other long-term assets		25,057,995.16	23,957,038.13	59,829,541.79	59,480,277.79
Cash paid for investments		14,298,170.60	14,298,170.60	—	9,008,212.50
Other cash paid relating to investment activities		—	—	—	—
<b>Sub-total of cash outflows from investment activities</b>		<b>39,356,165.76</b>	<b>38,255,208.73</b>	<b>59,829,541.79</b>	<b>68,488,490.29</b>
<b>Net cash flow from investment activities</b>		<b>84,042,726.30</b>	<b>85,129,987.33</b>	<b>(56,010,236.79)</b>	<b>(64,669,185.29)</b>

# FINANCIAL REPORT

(PREPARED UNDER PRC ACCOUNTING STANDARDS)

Unit: RMB

Item	Notes	First half of 2007		First half of 2006	
		Consolidated	Parent company	Consolidated	Parent company
<b>3. Cash flows from financing activities:</b>					
Cash received from acquisition of investments		—	—	3,002,737.50	—
Including: Cash received from minority shareholders by subsidiaries		—	—	3,002,737.50	—
Cash received from borrowings		29,525,100.00	29,525,100.00	—	—
Other cash received relating to financing activities		—	—	13,237,408.32	13,237,408.32
<b>Sub-total of cash inflows from financing activities</b>		<b>29,525,100.00</b>	<b>29,525,100.00</b>	<b>16,240,145.82</b>	<b>13,237,408.32</b>
Cash repayments of debts		136,990,801.70	129,525,100.00	65,822,706.90	65,822,706.90
Cash payment for distribution of dividends, profits or interest expenses		6,093,895.10	5,975,596.05	22,376,057.65	22,376,057.65
Other cash paid relating to financing activities		—	—	—	—
<b>Sub-total of cash outflows from financing activities</b>		<b>143,084,696.80</b>	<b>135,500,696.05</b>	<b>88,198,764.55</b>	<b>88,198,764.55</b>
<b>Net cash flows from financing activities</b>		<b>(113,559,596.80)</b>	<b>(105,975,596.05)</b>	<b>(71,958,618.73)</b>	<b>(74,961,356.23)</b>
<b>4. Effect of changes in foreign exchange rate on cash and cash equivalents</b>		<b>(512,470.04)</b>	<b>(360,569.42)</b>	<b>—</b>	<b>—</b>
<b>5. Net increase in cash and cash equivalents</b>		<b>48,755,925.92</b>	<b>43,058,188.37</b>	<b>(121,716,740.64)</b>	<b>(135,770,949.58)</b>
Add: Balance of cash and cash equivalents at beginning of the period		133,134,361.19	104,613,535.66	298,041,418.46	282,395,883.76
<b>6. Balance of cash and cash equivalents at the end of the period</b>		<b>181,890,287.11</b>	<b>147,671,724.03</b>	<b>176,324,677.82</b>	<b>146,624,934.18</b>

## STATEMENT OF CASH FLOW FOR THE PERIOD SUPPLEMENTARY INFORMATION

Unit: RMB

Item	Notes	First half of 2007		First half of 2006	
		Consolidated	Parent company	Consolidated	Parent company
1. RECONCILIATION OF NET INCOME TO CASH FLOWS FROM OPERATING ACTIVITIES					
Net income		18,846,016.48	34,226,345.72	12,279,060.65	12,283,900.59
Add: Minority profit		3,193,606.52	—	(64,582.55)	—
Provisions for impairment of assets		5,807,587.78	(7,500,000.00)	—	—
Depreciation of fixed assets, depreciation of fuel assets and depreciation of biological assets for production		50,150,725.26	47,348,905.50	49,643,471.56	48,615,363.80
Amortization of intangible assets		1,976,477.12	1,954,077.00	2,036,224.00	2,036,224.00
Amortization of long-term prepayments		—	—	—	—
Losses on disposal of fixed assets, intangible assets and other long-term assets		(4,746,758.05)	(4,845,837.19)	(49,875.71)	(49,875.71)
Losses on scrapping of fixed assets		—	—	—	—
Losses on change of fair value		(1,961,740.72)	(1,961,740.72)	—	—
Financial expenses		10,668,099.17	10,144,995.94	10,396,691.36	10,147,321.50
Investments losses		(2,408,608.83)	(2,417,892.02)	(2,387,287.78)	(2,242,315.92)
Decrease in deferred tax assets		89,533.43	—	—	—
Increase in deferred tax liabilities		—	—	—	—
Decrease in inventories		2,192,789.50	49,367,044.22	31,965,582.42	34,960,965.33
Decrease in operating receivables		(117,689,424.55)	(173,581,434.93)	(15,341,604.41)	(8,911,684.28)
Increase in operating payables		112,666,963.35	111,529,902.99	(82,225,564.66)	(92,980,307.37)
Others		—	—	—	—
NET CASH FLOWS FROM OPERATING ACTIVITIES		78,785,266.46	64,264,366.51	6,252,114.88	3,859,591.94
2. INVESTING AND FINANCING ACTIVITIES THAT DO NOT INVOLVE CASH RECEIPTS AND PAYMENTS					
Conversion of debt into capital		—	—	—	—
Convertible bonds to be expired within one year		—	—	—	—
Fixed assets under finance lease		—	—	—	—
3. NET INCREASE IN CASH AND CASH EQUIVALENTS					
Balance at the end of this period in cash and cash equivalents		181,890,287.11	147,671,724.03	176,324,677.82	146,624,934.18
Less: balance at the begin of this period in cash and cash equivalents		133,134,361.19	104,613,535.66	298,041,418.46	282,395,883.76
NET INCREASE IN CASH AND CASH EQUIVALENTS		48,755,925.92	43,058,188.37	(121,716,740.64)	(135,770,949.58)

# FINANCIAL REPORT

(PREPARED UNDER PRC ACCOUNTING STANDARDS)

## STATEMENT OF SHAREHOLDERS'EQUITY CHANGE (consolidated)

Unit: RMB

Item	Balance of this period								
	Equity attributable to holders of parent company						Others	Minority shareholders' equity	Total shareholders' equity
	Share capital	Capital surplus	Less: treasury Share	Surplus reserve	General risk provision	Undistributed profit			
1. Balance at the end of prior year	457,312,830.00	558,919,077.15		162,285,764.68		165,397,982.84	(578,694.36)	3,312,522.34	1,346,649,482.65
Add: Change in accounting policy						6,896,010.76	1,286,810.15		8,182,820.91
Correction of prior mistakes									—
2. Balance at the beginning of this year	457,312,830.00	558,919,077.15	—	162,285,764.68	—	172,293,993.60	708,115.79	3,312,522.34	1,354,832,303.56
3. Changes of funds of this year									
(minus "-")	—	67,891,962.00	—	—	—	9,699,759.88	(11,014.40)	22,174,378.30	99,755,085.78
(1) Net profit						18,846,016.48		3,193,606.52	22,039,623.00
(2) Profit and loss directly accounted for in shareholders' equity	—	67,891,962.00	—	—	—	—	(11,014.40)	—	67,880,947.60
1) Net change in fair value of financial assets available for sale		67,891,962.00							67,891,962.00
2) Effect of changes in other shareholders' equity of investee units under equity method									—
3) Effect of income tax on items including shareholders' equity									—
4) Others							(11,014.40)		(11,014.40)
Subtotal of item (1) and (2) above	—	67,891,962.00	—	—	—	18,846,016.48	(11,014.40)	3,193,606.52	89,920,570.60
(3) Shareholders' investment and	—	—	—	—	—	—	—	18,980,771.78	18,980,771.78
1) Appropriation of surplus reserve									—
2) Appropriation of general risk provision									—
3) Distribution to shareholders								18,980,771.78	18,980,771.78
(4) Profit Distribution	—	—	—	—	—	(9,146,256.60)	—	—	(9,146,256.60)
1) Appropriation of surplus reserve									—
2) Appropriation of general risk provision									—
3) Distribution to shareholders						(9,146,256.60)			(9,146,256.60)
4) Others									—
(5) Internal transfer of shareholders' equity	—	—	—	—	—	—	—	—	—
1) Transfer of capital reserve to increase share capital									—
2) Transfer of surplus reserve to increase share capital									—
3) Surplus reserve to make up losses									—
4) Others									—
4. Balance at the end of this period	457,312,830.00	626,811,039.15	—	162,285,764.68	—	181,993,753.48	697,101.39	25,486,900.64	1,454,587,389.34



Unit: RMB

Item		Balance of last year								
		Equity attributable to holders of parent company						Minority shareholders' equity	Total shareholders' equity	
		Share capital	Capital surplus	Less: treasury Share	Surplus reserve	General risk provision	Undistributed profit			Others
1.	Balance at the end of prior year	457,312,830.00	558,919,077.15		160,207,660.67		167,636,170.49	(583,121.59)	1,091,928.47	1,344,584,545.19
	Add: Change in accounting policy						5,632,026.23	1,027,247.49		6,659,273.72
	Correction of prior mistakes									—
2.	Balance at the beginning of this year	457,312,830.00	558,919,077.15	—	160,207,660.67	—	173,268,196.72	444,125.90	1,091,928.47	1,351,243,818.91
3.	Changes of funds of this year (minus “-”)	—	—	—	—	—	(10,586,580.85)	212,022.18	2,938,154.95	(7,436,403.72)
	(1) Net profit						12,279,060.65		(64,582.55)	12,214,478.10
	(2) Profit and loss directly accounted for in shareholders' equity	—	—	—	—	—	—	212,022.18	—	212,022.18
	1) Net change in fair value of financial assets available for sale									—
	2) Effect of changes in other shareholders' equity of investee units under equity method									—
	3) Effect of income tax on items including shareholders' equity									—
	4) Others							212,022.18		212,022.18
	Subtotal of item (1) and (2) above				—	—	12,279,060.65	212,022.18	(64,582.55)	12,426,500.28
(3)	Shareholders' investment and	—	—	—	—	—	—	—	3,002,737.50	3,002,737.50
	1) Appropriation of surplus reserve								3,002,737.50	3,002,737.50
	2) Appropriation of general risk provision									—
	3) Distribution to shareholders									—
(4)	Profit Distribution	—	—	—	—	—	(22,865,641.50)	—	—	(22,865,641.50)
	1) Appropriation of surplus reserve									—
	2) Appropriation of general risk provision									—
	3) Distribution to shareholders						(22,865,641.50)			(22,865,641.50)
	4) Others									—
(5)	Internal transfer of shareholders' equity	—	—	—	—	—	—	—	—	—
	1) Transfer of capital reserve to increase share capital									—
	2) Transfer of surplus reserve to increase share capital									—
	3) Surplus reserve to make up losses									—
	4) Others									—
4.	Balance at the end of this period	457,312,830.00	558,919,077.15	—	160,207,660.67	—	162,681,615.87	656,148.08	4,030,083.42	1,343,807,415.19

## NOTES TO THE ACCOUNTS (UNLESS OTHERWISE INDICATED, ALL FIGURES ARE STATED IN RMB'000)

### 1. BACKGROUND OF THE COMPANY

Shandong Xinhua Pharmaceutical Company Limited (hereinafter referred to as the “Company”) was established in 1993 pursuant to the reorganization of Shandong Xinhua Pharmaceutical Factory. The Company issued its H Shares in the Hong Kong Stock Exchange in December 1996 and listed its A Shares in the Shenzhen Stock Exchange in July 1997. The Company became a foreign invested joint stock company in November 1998 upon approval by the Ministry of Foreign Trade and Economic Cooperation of the PRC. The Company issued an additional 30 million ordinary A shares as approved and decreased 3 million state-owned shares in September 2001. In accordance with the revised share reform of the Company in June 2006 for the conversion of non-tradable A shares to tradable A shares (the “Revised Share Reform”) the holder of the non-tradable A shares, Shandong Xinhua Pharmaceutical Group Company Limited (“SXPGC”), which was also an immediate holding company of the Company, offered as consideration, 3.5 shares of non-tradable A shares of the Company for every 10 tradable A Shares held by A share shareholders as registered on the registration date in respect of the implementation of the Revised Share Reform. Upon the completion of the proposal, SXPGC offered 26,653,665 non-tradable A shares as condition to have trading rights in the A share market.

The registered capital of the Company as of 30 June 2007 is RMB457.31 million and its share capital as of 30 June 2007 consists of the following:

	No. of Shares	Amount	Ratio
State-owned shares	163,259	163,259	35.70%
Legal person shares	24,527	24,527	5.36%
Senior management-held shares	34	34	0.01%
Publicly held H shares	150,000	150,000	32.80%
Publicly held A shares	119,493	119,493	26.13%
Total	<u>457,313</u>	<u>457,313</u>	<u>100%</u>

The Company is mainly engaged in developing, manufacturing and selling bulk pharmaceuticals, preparations and chemical products.

According to the circular “Lu Ke Gao Zi (2001) No. 647” issued by the Shandong Provincial Bureau of Science & Technology, the Company has been recognized as a new and high-tech company.

The Company’s place of registration is the Chemical Area in Zibo New and High Technology Industrial Development Zone, Shandong Province.

### 2. BASIS OF PRESENTATION

- 1 Financial statements have been prepared in conformity with the Accounting Principles for Business Enterprises and its application guides promulgated by the Ministry of Finance of the PRC (“MOF”).
- 2 Methods of preparing consolidated financial statements
  - 2.1 Scope of consolidation: The consolidated financial statements include the financial statements of the Company and its subsidiaries in which the Company holds 50% or more of the voting capital, or holds less than 50% of the voting capital but has substantial control over them.
  - 2.2 Consolidated financial statements have been prepared in accordance with No. 33 the Accounting Principles for Business Enterprises about Consolidated Financial Statements and relevant supplementary regulations issued by the MOF. All significant transactions and balances between the Company and its subsidiaries are eliminated for the purpose of consolidation.

### 3. SIGNIFICANT ACCOUNTING POLICIES AND ACCOUNTING ESTIMATES

#### 1 Statement in accordance with the Accounting Principles for Business Enterprises

Financial statements have been prepared in conformity with the Accounting Principles for Business Enterprises and its application guides promulgated by the MOF. According to the requirements of the “public offering of securities of companies standardize information disclosure Quiz No. 7 — old and new accounting standards during the transition period will be more financial or the preparation of the information and disclosure”, the Company has adjusted related matters.

#### 2 Accounting year

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

#### 3 Principles of Accounting and basis of valuation

Financial statements have been prepared on an accrual basis and all assets are stated at actual cost of acquisition unless otherwise indicated.

#### 4 Reporting currency

The Company's reporting currency is Renminbi (“RMB”).

#### 5 Foreign currency translation

Foreign currency transactions for the year are translated into RMB at the exchange rate as quoted by the People's Bank of China on the first day of the month in which the transactions occurred. Foreign currency monetary assets and liabilities are translated into RMB at the prevailing exchange rate as at the balance sheet date. The resulting exchange differences are accounted for as exchange gains or losses of the period, the differences arising from the organization period are accounted for as long-term prepaid expenses, and the difference arising from borrowings related to the acquisition or construction of a fixed asset are treated according to the Principle of Capitalization of Borrowing Costs.

#### 6 Cash equivalents

Cash equivalents are short-term (usually due within three months from the date of purchase), highly liquid investments that are readily convertible to known amounts of cash and subject to an insignificant risk of change in value.

#### 7 Translation of Financial assets

##### 7.1 Classification of Financial assets

Financial assets of the Company can be classified into:

- (1) Financial assets at fair value through profit or loss, including financial assets for trading and financial assets designated to be measured at fair value through profit or loss;
- (2) Held-to-maturity investment;
- (3) Loans and accounts receivables;
- (4) Financial assets available for sale.

**7.2 Measurement of Financial assets**

- 7.2.1 Financial assets upon initial recognition are measured at fair value. For financial assets measured at fair value through profit or loss, trading fees thereof are to be directly included in profit or loss; whereas that of financial assets of other classes are to be included in amounts initially recognized.
- 7.2.2 The Company conducts subsequent measurement of financial assets in accordance with the fair value without deducting trading fees possibly attributable to disposal of the financial assets in the future, save as follows:
- (1) Held-to-maturity investment and loans and accounts receivables are carried at amortized cost by effective interest method.
  - (2) Investment of equity instruments of which there are no quotations in active market and no reliable measurement of the fair value, plus equity instruments linked derivative financial assets which must be cleared through delivery of equity instruments are carried at cost.

**7.3 Recognition of the fair value of financial assets**

- 7.3.1 The fair value of financial assets where there is active market will be determined by quotations in the active market.
- 7.3.2 The fair value of financial assets where there is no active market will be determined by valuation techniques. The outcome of applying valuation techniques reflects the trading price which may be adopted in an arm's length transaction on the valuation date.

**7.4 Impairment of Financial Assets**

The book value of financial assets other than those at fair value through profit or loss is assessed on the balance sheet date. Provisions for impairment should be made when there is objective evidence of impairment on the financial assets. Objective evidence supporting impairment on financial assets mainly include the followings:

- (1) Issuers or debtors are under severe financial difficulties;
- (2) Any breach of terms of contract by debtors, such as a breach of contract or let the payment falls overdue in the settlement of interest or principal;
- (3) Debtors give way to those under financial difficulty accounting on economic or legal reasons;
- (4) Debtors may go into liquidation or conduct other financial reorganization;
- (5) Transaction of the financial assets ceases in the active market as the issuer encounters great financial difficulties;
- (6) Any reduction in cash flow of certain assets among a group of financial assets cannot be identified, while it is discovered that the expected future cash flow of the financial assets has been reduced and can be measured since initial recognition after an overall evaluation based on disclosed information. If the repayment capability of the debtor of the group of financial assets gradually deteriorates, unemployment rate of the country or region where the debtor is staying increases, prices in regions where collaterals are provided significantly decrease or an industry sentiment turns unfavorable ;
- (7) Significant and adverse changes have taken place in the technological, market, economic or legal environments in which the debtor operates, making investors of equity instruments difficult to recover the investment cost;
- (8) Substantial or non-temporary reduction of the fair value of investment on equity instruments;
- (9) Other objective evidence which shows impairment on financial assets.

**7.5 Measurement of impairment loss on financial assets**

- 7.5.1 Financial assets at fair value through profit or loss need not be tested for impairment;
- 7.5.2 Measurement of impairment loss on held-to-maturity investment: provisions are made for impairment with reference to the differences between the present value of expected future cash flow and book value.
- 7.5.3 For financial assets available for sale and can be measured reliably, provisions for impairment are made and reported in profit or loss by the amount of book value in excess of fair value. For those that cannot be measured reliably, provisions for impairment are made and reported in profit or loss by the amount of book value in excess of the present value of expected future cash flow. Accumulated loss incurred due to a reduction of fair value has to be transferred out and be reported in profit or loss instead of being directed accounted for in shareholders' equity when financial assets available for sale impair, even though recognition of those financial assets has not yet ceased.
- 7.5.4 Measurement of impairment loss on accounts receivables: impairment loss of accounts receivables of the Company and provisions for bad debts are recognized and made with reference to the aging of accounts receivables and the claim quota as required on an aging basis. Provision for bad debts losses are usually made as follows:

<b>Aging</b>	<b>Bad debts percentage</b>
Less than 1 year	0.5%
1 to 2 years	20%
2 to 3 years	60%
Over 3 years	100%

Provision for bad debts losses of other receivables is made in the same way as for accounts receivable. Provision for special receivables is made after assessing their collectibility.

Accounts receivables from related parties are always not made for any provision. Accounts receivables that cannot be recovered has been written off as bad debt losses after approval by the board of directors or shareholders in general meeting, and reported as reductions of provision for doubtful accounts.

**8 Inventories**

Inventories mainly include raw materials, work-in-process, finished products, goods in stock, low-value consumables and packaging materials.

- 8.1 Raw materials are stated at the cost of purchase price plus freight, loading and unloading charges, and insurance premiums. The cost of self-made semi-products and finished products include various expenditures actually incurred during production.
- 8.2 The valuation of raw materials, self-made semi-products and finished products is made on a weighted-average basis when they are shipped and sold.
- 8.3 Low-value-consumables and packaging materials are expensed as incurred.
- 8.4 Inventories are stated at the lower of cost or market value at the end of the period. When the cost of inventories is higher than their recoverable amount because they are damaged, completely or partially obsolescent, or with a selling price lower than the cost, a provision for inventory write-down is made after a thorough examination of inventories at the end of the period. The provision is made on the difference between the cost of inventory items and their lower net realizable value on an item-by-item basis. Net realizable value refers to the amount of an estimated selling price less the estimated costs of completion and estimated selling expenses and taxes.

**9 Long-term equity investment****9.1 Initial measurement**

9.1.1 The initial investment cost of long-term equity investment from combinations of entities are determined according to the following requirements:

- (1) For combinations of entities under common control in which a company pays cash, transfers non-cash assets or bear debts as consideration of combinations, the initial investment cost of long-term equity investment are the share with reference to the book value of the shareholders' equity of the party to be combined on the date of combinations. Capital reserve account is adjusted by differences between initial investment cost of long-term equity investment and the book value of the cash paid, non-cash assets transferred as well as liabilities assumed. Amounts that cannot be sufficiently released by capital reserve account serve the purpose of adjusting retained earnings. For companies offering consideration of combinations by issuing equity securities, initial investment cost of long-term equity investment refers to the share with reference to the book value of the shareholders' equity of the party to be combined on the date of combinations, which becomes share capital with reference to the nominal value of shares in issue. Capital reserve account is adjusted by differences between initial investment cost of long-term equity investment and the aggregate nominal value of shares in issue. Amounts that cannot be sufficiently released by capital reserve account serve the purpose of adjusting retained earnings.
- (2) For combinations of entities without common control, initial investment cost of long-term equity investment refers to the assets paid, liabilities incurred or assumed as well as the fair value of equity securities in issue by the company in exchange for control of the acquiree on the date of acquisition, plus fees directly attributable to combinations of entities. Differences between the fair value and the book value hereof are included in profit or loss.

9.1.2 For long-term equity investment settled in cash, initial investment cost refers to the actual consideration paid. Initial investment cost is comprised of fees directly attributable to the acquisition of long-term equity investment, tax and other necessary expenses.

9.1.3 Initial investment cost refers to long-term equity investment acquired through the issue of equity securities in accordance with the fair value of equity securities in issue.

9.1.4 Save for unfair agreed value under contract or agreement, initial investment cost are long-term equity investment of investors with reference to the agreed value stipulated under investment contract or agreement.

**9.2 Subsequent Measurement**

9.2.1 The following long-term equity investment is translated by cost method:

- (1) Enterprises can invest in long-term equity controlled by investee. Investee are subsidiaries of the controlling enterprise, and are consolidated in the combined financial statement. Long-term equity investment in subsidiaries is translated by cost method, subject to adjustment pursuant to equity method during preparation of the combined financial statement.
- (2) Not only can an enterprise be eligible for joint control or excising material impacts on the investee, but can also invest in long-term equity without quotations in active market together with a fair value that cannot be reliably measured.

9.2.2 Long-term equity investment with joint control or material impact on the investee is accounted for using equity method.

9.2.2.1 Original cost of long-term equity investment which is greater than its share of fair value of the investee's identifiable net assets is stated without adjustment. The shortfall of the original cost from its share of fair value of the investee's identifiable net assets is credited to the current profit and loss account with an adjustment to the cost of the long-term equity investment.

9.2.2.2 After long-term equity investment is acquired, the gain or loss from investment shall be recognised with an adjustment to the book value of long-term equity investment according to its share of the investee's net profit or loss for the period. The book value of long-term equity investment is reduced based on its share of the investee's profit or cash dividends as declared.

9.2.2.3 The net loss from the investment in investee is reorganised to the extent that the book value of the long-term equity investment and other long-term interest in substance in the investee are written down till nil, unless the investor is under an obligation to bear additional loss. In the event that net profit is recorded by the investee in the future, recognition of the investor's share of the investee's net profit may be resumed after recovering its share of unrecognised loss.

9.2.2.4 The investor's share of the investee's net profit and loss is recognised based on the fair value of identifiable assets of the investee upon acquisition of the investment, subject to an adjustment to the investee's net profit. The financial statements of the investee are subject to adjustment where there is a difference in the accounting policies and accounting periods adopted by the investee with those of the investor in accordance with the latter, upon which the investment gain or loss from the investment is recognised.

9.2.2.5 Changes in shareholders' equity other than the share of the investee's net profit and loss are accounted for with an adjustment to the book value of the long-term equity investment and included into shareholders' equity. Long-term equity investment in an investee over which the investor ceases to have joint control or material impacts due to divestment or other reasons, without public quotation in an active market and a fair value to be measured reliably is accounted for using cost method instead, where the book value of long-term equity investment under equity method is deemed as the original cost of the investment to be accounted for through cost method. Long-term equity investment in an investee over which the investor is eligible for joint control or excising material impacts, yet constituting no control, due to additional investment or other reasons is accounted for using cost method instead, where the book value of long-term equity investment under the cost method is deemed as the original cost of the investment to be accounted for through equity method.

### 9.3 Recognition standards and provision methods for impairment of long-term equity investment

At the end of each year, a provision for impairment of the long-term equity investment is made for any difference arising between the recoverable amount of long-term equity investment and its book value.

## 10 Fixed assets and construction-in-progress

### 10.1 Fixed assets

10.1.1 Fixed assets include buildings, machinery equipment, and transportation equipment. Fixed assets are assets with a useful life over one year, such as buildings and other major equipment used in production, and those that are not major equipment used in production but with a unit value of over RMB2,000 and useful life of over 2 years.

10.1.2 Fixed assets are recorded at the cost of acquisition. The cost of fixed assets purchased include the purchasing price, value added tax ("VAT"), import duty, and other expenditures necessary to bring the fixed assets into their usable conditions. Fixed assets invested by investors are recorded at an amount as agreed upon by all the investors concerned.

10.1.3 Fixed assets (excluding those fully depreciated yet still used in operation) are depreciated on a straight-line basis with the estimated net residual value at 5%. The life and rate of depreciation for different classes of fixed assets are as follows:

Items	Useful life	Annual depreciation rate
Buildings & constructions	20 Years	4.75%
Machinery & equipment	10 Years	9.5%
Electronic apparatus	5 Years	19%
Office equipment and vehicles	5 Years	19%

10.1.4 The Company provides for impairment of the fixed assets that are actually impaired (e.g., because of excessive capacity, longtime inefficient utilization, significant decrease in replacement value, return on fixed assets much lower than the normal return of funds), based on the excess of the carrying amount of the assets over their realizable value. Provision for impairment of fixed assets is made in the following events:

- (1) The market value of fixed assets has declined significantly more than expected as a result of passage of time or normal use and the declined value is not expected to be recovered in the near future;
- (2) Fixed assets have become obsolete or physically damaged;
- (3) Significant adverse changes in the expected utilization of fixed assets with a negative effect on the Company, including the Company's plans to discontinue or restructure the operation to which the fixed assets belong, or to dispose of the fixed assets before the originally expected dates;
- (4) Significant changes with an adverse effect on the Company have taken place or will take place in the near future in the technological, market, economic or legal environments in which the Company operates, or in the market to which the products are dedicated;
- (5) Market interest rates have increased significantly in the period and the increases are likely to affect the discount rate used in calculating the assets' recoverable amount and therefore decrease the fixed assets' recoverable amount to a material extent;
- (6) Other situations that indicate the impairment of fixed assets.



**10.2 Construction in progress**

- 10.2.1 The cost of construction-in-progress is determined according to expenditures actually incurred. The cost of construction work undertaken by the Company itself is determined according to direct materials cost, direct labor cost, 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 test run expenses.
- 10.2.2 Construction in progress is transferred to fixed assets at the date of reaching its usable conditions at an estimated amount based on the budget price, the amount paid to the contractor or actual cost of construction. The asset will be depreciated from the second month after it is put into use. The estimated value of the asset and its accumulated depreciation is adjusted after going through the procedures for the final accounts of project completion.
- 10.2.3 The Company conducts a thorough inspection of construction-in-progress at the year-end and makes a provision for impairment on any excess of the carrying amount of construction-in-progress over its recoverable amount on an item-by-item basis on occurrence of one or several of the following situations:
- (1) Construction-in-progress suspended for quite a long time and not to be resumed within 3 years;
  - (2) Construction-in-progress is obsolete in terms of function and technology, and there is great uncertainty of bringing economic benefits to the Company;
  - (3) Other situations indicating the impairment of construction-in-progress.

**11 Properties Held-for-investment**

- 11.1 Recognition scope for properties held-for-investment: leased land use rights; land use rights held for sale after appreciation; leased buildings.
- 11.2 Initial Measurement Method for Properties Held-for-investment: The properties held-for-investment are initially stated at cost. The cost of purchased properties held-for-investment includes purchase price, relevant taxes and surcharges and other expenses which are directly attributable to the asset. The cost of self-constructed properties held-for-investment comprises necessary expenditures incurred in construction to bring the asset to its working condition. The cost of properties held-for-investment otherwise acquired is recognised in accordance with relevant accounting standards.
- 11.3 Subsequent Measurement Method for Properties Held-for-investment: The cost model is adopted for subsequent measurement of properties held-for-investment and the straight-line method is used for depreciation.

**12 Borrowing costs**

- 12.1 Borrowing costs include interests incurred by the Company in connection with the borrowings, amortization of premium or discount-plus auxiliary expenses, and foreign exchange translation differences from foreign currency borrowings. Other borrowing costs, except for special borrowing costs incurred from the acquisition or construction of a fixed asset, is charged directly as financial expenses in the period incurred. Special borrowing costs incurred from acquisition or construction of a fixed asset are capitalized when the following three conditions are fully satisfied:
- (1) Expenditures for the asset are being incurred;
  - (2) Borrowing costs are being incurred; and
  - (3) Acquisition and construction that are necessary to enable the asset reach its expected usable condition have commenced.
- 12.2 The borrowing costs incurred for an asset acquired or constructed in compliance with the above conditions is capitalized before the asset has reached its expected usable condition and is charged as financial expenses after the asset has reached its expected usable condition.

**13 Valuation and amortization of intangible assets**

- 13.1 Intangible assets are recorded at the actual cost of 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 the expenses for internal research and development projects of the Company are divided into expenses in the research phase and expenses in the development phase. Research refers to scheduled innovative investigations to obtain and understand scientific or technological knowledge. The expenses in the research phase are charged to the current profit and loss account. Development means to apply the research outcomes or other knowledge to a plan or design prior to a commercial production or use in order to produce new or essentially-improved materials, devises, products, etc. The expenses in the development phase, if so qualified, are recognised as intangible assets.
- 13.2 The cost of intangible assets of the Company is amortized evenly over the amortization period not 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. Intangible assets are amortized from the month of acquisition. The amortization period shall not exceed 10 years given the lack of any specification in the contract or by law. The Company's intangible assets include land use rights, patents, non-proprietary technologies, and trademarks etc. The land use right is amortized over a period of 50 years, and the software use right is amortized over a beneficial period of 5 years.
- 13.3 The Company provides for impairment of intangible assets impairment for the excess of the carrying amount of the asset over its recoverable amount on occurrence of one or several of the following circumstances:
- (1) An intangible asset has been replaced by a new technology and its ability to bring economic benefits to the Company has been adversely affected;
  - (2) A drastic decline in the market value of an intangible asset occurred during the period is not likely to be recovered during the remaining amortization period;
  - (3) An intangible asset whose legal protection period has expired but can still be used to a certain extent; and
  - (4) Other circumstances indicating the impairment of intangible asset.

## 14 Revenue Recognition

The Company's operating revenue is mainly derived from sale of goods revenue. Revenue is recognized when the Company 1) has transferred to the buyer the substantial risks and rewards of ownership of the goods, 2) neither retains continuing managerial involvement nor exercises control over the goods sold, 3) has received or obtained evidence of payment, and 4) the relevant costs can be measured reliably.

## 15 Accounting of Income Tax

The Company applies the balance sheet liability method for accounting of income tax.

- 15.1 The tax bases of acquired assets or liabilities are determined upon their acquisition by the Company. Where there is difference between the carrying amount of assets or liabilities and the tax bases, the deferred income tax assets or the deferred income tax liabilities arising therefrom are recognised. The differences between the carrying amount of assets or liabilities and the tax bases are recognised as temporary differences, which are classified as taxable temporary differences and deductible temporary differences.
- 15.2 The unpaid income taxes payable in the current period and in the preceding periods are recognised as liabilities, and the excess of paid income taxes over the payables is recognised as assets by the Company. A taxable temporary difference or deductible temporary difference is recognised as deferred income tax liabilities or deferred income tax assets respectively.
- 15.3 Deferred income tax assets arising from deductible temporary differences are recognised by the Company to the extent that it is probable that future taxable profit will be available against which the deductible temporary differences can be utilised. 15.4 The current income tax and the deferred income tax of the Company are included in the current profit and loss account as income tax expenses or gains.
- 15.4 Current income tax and deferred income tax are calculated into current profit/loss as taxation expense.

## 16 Accounting Policies and Changes in Accounting Estimates

The Company has fully implemented the system and relevant regulations of the new Accounting Standards for Business Enterprises promulgated by the Ministry of Finance from 1 January 2007, pursuant to which certain amendments were made to the accounting policies of the Company. In preparing the comparative financial statements of the Company, retrospective adjustments have been made to related events in accordance with Q&A No. 7 regarding Rules on Information Disclosure of Publicly-listed Companies - Preparation and Disclosure of Comparative Financial Information during the Transitional Period of Existing and New Accounting Standards. The beginning and ending amounts of equity attributable to holders of parent company increased RMB8,183,000 and RMB77,947,000 respectively because of the implementation of the new Accounting Standards for Business Enterprises.

**4. TAXES**

Major taxes and tax rates applicable to the Company are as follows:

**1 Income tax**

According to the document (State Revenue Issue [1994] No. 151 “The Notice of Applying favourable tax policies for the new and high technology companies”) issued by the State Bureau of Revenue, the Company is subject to an income tax rate of 15% starting from 2002 because its place of registration is the Chemical Zone in Zibo Municipal New and High Technology Industrial Development Zone, Shandong Province, and approved by the local department of revenue. The Company is subject to 15% income tax for operating income generated from the development zone and 33% income tax for operating income generated outside the development zone from 2004, and has put on records in the local department of revenue.

Zibo Xinhua-Perrigo Pharmaceutical Co. Ltd, a company in which the Company holds a controlling interest, is subject to 24% income tax, while the other subsidiaries of the Company are subject to 33% income tax.

**2 Value added tax**

The Company is subject to value added tax for its sales revenue at a VAT rate of 17% or 13% for domestic sales and 0% for export sales.

For the purchase of raw materials, the input VAT is deductible against output VAT at the rate of 17%.

The VAT payable for the period is the amount of output VAT less input VAT.

**3 Business tax**

Business tax is based on the design revenue and leasing revenue, at a rate of 5%.

**4 Urban maintenance and construction tax and education surcharges**

Urban maintenance and construction tax and education surcharges are based on the sum of VAT payable and sales tax payable, at the rates of 7%, 3% and 1% respectively.

**5 Property tax**

Property tax is levied based on 70% of the original cost of the building property of the Company at a rate of 1.2%. The Company is subject to a 12% tax rate for rental income from leasing its building property.

## 5. MAJORITY-OWNED SUBSIDIARIES, JOINT COMPANY AND ASSOCIATES

## 1 As of 30 June 2007, the detailed list of the majority-owned subsidiaries and associates of the Company is as follows:

Number	Company name	Registered capital	Amount	Ratio	Principal operations	Consolidated or not
1	Zibo Xinhua Drug Store Chain Company Limited	RMB2,000,000	RMB1,760,000	88%	Retail of pharmaceuticals	Y
2	Zibo Xinhua Sanhe Chemical & Industrial Company Limited	USD500,000	USD350,000	70%	Research, production & sale of pharmaceuticals & chemicals	Y
3	Zibo Xinhua Pharmaceutical Design Institute	RMB2,000,000	RMB1,800,000	90%	Pharmaceutical project design	Y
4	Dongying Xinhua Pharm. Company Limited	RMB900,000	RMB477,000	46.64%	Retail of pharmaceuticals	Y
5	Shandong Xinhua Pharmaceutical (European) GmbH	EUR650,000	EUR500,000	76.9%	Bulk pharmaceutical and intermediates operation	Y
6	Zibo Xinhua – Perrigo Pharmaceutical Company Limited	USD6,000,000	USD3,006,000	50.10%	Production & sale of Ibuprofen materials	Y
7	Shandong Xinhua Pharmaceutical Trade Company Limited	RMB48,498,900	RMB47,528,900	99.76%	Drug sale	Y
8	Zibo Xinhua-Eastwest Pharmaceutical Company Limited	USD1,500,000	USD1,125,000	75%	Production and sale of calcium polycarboxyl materials	Y
9	Shandong Xinhua Pharmaceutical Import & Export Company Limited	RMB3,000,000	RMB660,000	99.52%	Import & export of cargos and technologies	Y
10	Shandong Xinhua Longxin Chemical & Industrial Company Limited	RMB25,000,000	RMB10,000,000	40%	Production and sales of Salicylic acid series (excluded dangerous and poisonous chemical)	N
11	Shandong Dadi Xinhua Chemical & Industrial Company Limited	RMB26,000,000	RMB12,740,000	49%	Production and sales of chemical products (excluded dangerous chemical)	N
12	Shandong Xinhua Changxing Chemical Equipment Company Limited	RMB22,000,000	RMB7,700,000	35%	Production and sales of chemical facilities and fittings	N
13	Shandong Zibo XinCat Pharmaceutical Company Limited	RMB26,928,800	RMB10,179,000	20%	Production preparations	N

1. Zibo Xinhua Drug Store Chain Company Limited (the name was changed from Zibo Xinhua Drug Store Company Limited in December 2003, hereafter referred to as the “Zibo Drug Store”) was incorporated in July, 1999 with the registered capital contributed by the Company and Xinhua Pharmaceutical Group Company Limited, which hold 88% and 12% of the equity interests, respectively. The original registered capital was RMB1,000,000 and it was increased to RMB2,000,000 in September 2002.
2. With a registered capital of USD500,000, Zibo Xinhua-Sanhe Chemical & Industrial Company Limited (hereinafter referred to as the “Sanhe Chemical”) was formed in October 2002 by the Company, Nippon Gonghe Pharmaceutical Company Limited and Beijing Santian Chemical Tech. Company Limited, which hold 70%, 25% and 5% of equity interests, respectively. In December 2005, Beijing Santian Chemical Tech. Company Limited transferred all the equities to Nippon Gonghe Pharmaceutical Company Limited and the equity structure thus has changed as: the Company and Nippon Gonghe Pharmaceutical Company Limited hold 70% and 30% of equity interests, respectively.
3. With a registered capital of RMB2,000,000, Zibo Xinhua Pharmaceutical Design Institute (hereinafter referred to as the “Design Institute”) was formed in March 2002 by the Company and Xinhua Pharmaceutical Group Company Limited, which hold 90% and 10% of the registered capital, respectively.

4. With a registered capital of RMB900,000, Dongying Xinhua Pharmaceutical Company Limited (hereinafter referred to as the “Dongying Pharmaceutical”) was formed in March 2002 by Zibo Xinhua Drug Store Chain Company Limited (a majority-owned subsidiary of the Company) and Dongying Lanjing Tech. Company Limited, which hold 53% and 47% of equity interests respectively.
5. Shandong Xinhua Pharmaceutical (European) GmbH (hereinafter referred to as the “Xinhua European”) was established on 25 November 2003. It was jointly invested by the Company and Mr. LI PENG from Germany. The registered capital was 1 million Euros. The Company holds 70% of equity interests, while Mr. LI PENG owns 30%. This company was incorporated in Hamburg, Germany. This company’s reporting currency is Euro. In July 2006, the registered capital of the Company was changed to EUR650,000 according to the resolution of the Board of Directors’ meeting, and the share of equity interest held by the Company and Mr. LI PENG was changed to 76.90% and 23.10% respectively.
6. Sino-USA Zibo Xinhua-Perrigo Pharmaceutical Company Limited (hereinafter referred to as the “Xinhua-Perrigo”) was established by the Company and Perrigo International Inc. on 11 September 2003. With a registered capital of USD6 million, the Company Perrigo International Inc. hold 50.10% and 49.90% equity interests respectively.
7. With a registered capital of RMB5 million, Shandong Xinhua Pharmaceutical Trade Company Limited was established on 30 August 2004 by the Company and Zibo Xinhua Drug Store Chain Company Limited (a majority-owned subsidiary of the Company), which hold 98% and 2% of the registered capital, respectively. In March 2005, the registered capital increased by RMB43,498,900, among which, RMB42,628,900 was contributed by the Company in tangible assets, and RMB870,000 was contributed by Zibo Xinhua Drug Store Chain Company Limited in cash. The share of equity interest held by each shareholder remains unchanged.
8. With a registered capital of USD1.5 million, Zibo Xinhua-Eastwest Pharmaceutical Company Limited (hereinafter referred to as “Xinhua-Eastwest”) was established on 15 November 2005 by the Company and Eastwest United Group, Inc., which hold 75% and 25% of the equity interests respectively, the principle operation of Zibo Xinhua-Eastwest Pharmaceutical Company Limited is producing and sales of Calcium Polycarbophil materials. On 26 June 2006, the Company and Eastwest United Group, Inc. injected USD1.125 million and USD0.375 million in cash respectively.
9. With a registered capital of RMB3 million, Shandong Xinhua Pharmaceutical Export & Import Company Limited (hereinafter referred to as “Xinhua Export& Import”) was established on 15 May 2006 by Shandong Xinhua Pharmaceutical Trade Company Limited and Zibo Xinhua Drug Store Chain Company Limited, which hold 98% and 2% of the equity interests respectively, the principle operation of Xinhua Export & Import is exporting & importing of goods and technology, entrepot & counter trade.
10. Shandong Xinhua Longxin Chemical & Industrial Company Limited (hereinafter referred to as the Xinhua Longxin) was established with the registered capital of RMB25,000,000 by the Company and Shandong Longxin Chemical & Industrial Company Limited on June 17, 2005. The Company contributes RMB10,000,000, accounting for 40% of the registered capital. The main business of Xinhua Longxin includes production and sale of Salicylic acid product series (excluded dangerous and poisonous chemical).
11. Shandong Dadi Xinhua Chemical & Industrial Company Limited (hereinafter referred to as the Dadi Xinhua) was established with the registered capital of RMB26,000,000 by the Company and Shandong Dadi Salt Chemical Group Company Limited on 12 September 2006. The Company contributes RMB12,740,000, accounting for 49% of the registered capital. The main business of Dadi Xinhua includes production and sale of chemical products (excluded dangerous and poisonous chemical).
12. Shandong Xinhua Changxing Chemical Equipment Company Limited (hereinafter referred to as the Xinhua Changxing) was established with the registered capital of RMB22,000,000 by the Company and Shandong Changxing Group Company Limited on 10 May 2006. The Company contributes RMB7,700,000, accounting for 35% of the registered capital. The main business of Xinhua Changxing includes production and sale of chemical facilities and fittings.

13. Shandong Zibo XinCat Pharmaceutical Company Limited (hereinafter referred to as the XinCat Pharmaceutical) was established on 21 March 1993. According to the equity transfer agreement of the Company and Zibo Zhongxing Investment Company Limited on 30 May 2007, the Company made an cash RMB10,179,000 to purchase 20% registered capital of XinCat Pharmaceutical, and the Company has enjoyed the 20% equity from XinCat Pharmaceutical received the first cash.

## 2 Change in scope of consolidation

As compared with last year, Zibo Xinhua-Perrigo Pharmaceutical Company Limited is consolidated into the consolidated accounting statement of the year. On 3 April 2006, the Company and Perrigo International Inc. signed Zibo Xinhua-Perrigo Pharmaceutical Company Limited Amendment Agreement for Equity Venture Contract and agreed mutually that Perrigo International Inc. would transfer 0.10% of the total equity interests of Zibo Xinhua-Perrigo Pharmaceutical Company Limited to the Company in a consideration of USD6,000. After the transferring of equity, the Company and Perrigo International Inc. would hold 50.10% and 49.90% of the equity interests, respectively. The Company has paid the consideration on 30 June 2007. Changes were made over business license registration of Xinhua Perrigo, which would be consolidated in the Reporting period. As changes were made in the scope of consolidated statement, the total assets of the Group increased by approximately RMB63,000,000 billion and operating revenues increased by approximately RMB53,000,000.

## 6. NOTES TO THE CONSOLIDATED ACCOUNT

### 1. Cash and Cash Equivalents

Item	2007.6.30	2006.12.31
Cash	115	184
Bank deposits	168,775	132,950
Other funds	70,000	29,401
Total	<u>238,890</u>	<u>162,535</u>
Including: Cash and cash equivalents	181,890	133,134

The end balance of other funds includes a sum of RMB57,000,000 (at the beginning of the year: RMB29,401,000) as bank acceptance deposit.

### 2. Trading Financial Assets

Item	2007.6.30	2006.12.31
Derivative financial assets	<u>2,095</u>	<u>134</u>

### 3. Notes Receivable

Item	2007.6.30	2006.12.31
Bank acceptance	<u>49,204</u>	<u>19,431</u>

The maturity date of notes receivable will be after June 2007. In the end balance there are no mortgaged, discounted or overdue notes receivable.

## 4. Accounts Receivable

Aging	2007.6.30	Ratio	Bad debts provision	2006.12.31	Ratio	Bad debts provision
Less than 1 year	274,439	79.57%	1,345	221,870	78.70%	101
1 to 2 years	39,499	11.45%	1,907	42,327	15.01%	2,744
2 to 3 years	23,993	6.96%	7,356	15,930	5.65%	8,032
Over 3 years	6,953	2.02%	6,953	1,814	0.64%	1,814
Total	<u>344,884</u>	<u>100.00%</u>	<u>17,561</u>	<u>281,941</u>	<u>100.00%</u>	<u>12,691</u>

In the end balance, there are no accounts receivable due from shareholders who hold 5% or more of the Company's voting rights.

## 5. Advances to Suppliers

Aging	2007.6.30	Ratio	2006.12.31	Ratio
Less than 1 year	38,946	99.34%	19,647	98.87%
1 to 2 years	172	0.44%	189	0.95%
2 to 3 years	87	0.22%	36	0.18%
Total	<u>39,205</u>	<u>100.00%</u>	<u>19,872</u>	<u>100.00%</u>

The end balance of advance payments does not have any advance payment due from shareholders who hold 5% or more of the Company's voting rights.

## 6. Other Receivables

Aging	2007.6.30	Ratio	Bad debts provision	2006.12.31	Ratio	Bad debts provision
Less than 1 year	28,842	63.72%	499	17,184	38.70%	10
1 to 2 years	3,344	7.39%	61	16,671	37.55%	166
2 to 3 years	3,120	6.89%	554	2,306	5.19%	533
Over 3 years	9,957	22.00%	2,614	8,239	18.56%	2,067
Total	<u>45,263</u>	<u>100.00%</u>	<u>3,728</u>	<u>44,400</u>	<u>100.00%</u>	<u>2,776</u>

In the end balance, there are no other receivables due from shareholders who hold 5% or more of the Company's voting rights.

## 7. Inventories

Item	2007.6.30	Provision for Impairment	2006.12.31	Provision for Impairment
Raw materials	47,711	—	31,458	—
Work-in-progress	29,729	—	67,456	—
Finished products	68,618	5,969	86,844	5,969
Goods in stock	69,583	760	32,410	1,168
Low-value consumables	11,653	—	11,727	—
Special materials for Government	1,598	—	1,597	—
Total	<u>228,892</u>	<u>6,729</u>	<u>231,492</u>	<u>7,137</u>

Inventories at the end of the period are not impaired except for finished products.



## 8. Financial Assets Available for Sale

Item	Fair value at 30 June 2007	Fair value at 31 December 2006
Ruiheng Pharm & Technology Investment Company Limited	3,200	3,200
Bank of Communications	82,117	13,577
Pacific insurance Company Limited	7,000	7,000
Total	<u>92,317</u>	<u>23,777</u>

## 9. Held-to-maturity Investments

Item	2007.6.30	2006.12.31
Qingdao Hisyn Trust & Investment Company Limited	—	117,000
Key construction fund of Zibo city	76	76
Total	<u>76</u>	<u>117,076</u>

## 10. Long-term Equity Investments

Name of investees	2007.6.30	2006.12.31
Sino-USA Zibo Xinhua-Perrigo Pharmaceutical Company Limited	—	19,027
Shandong Xinhua Longxin Chemical & Industrial Company Limited	11,115	10,694
Shandong Dadi Xinhua Chemical & Industrial Company Limited	13,108	5,300
Shandong Xinhua Changxing Chemical Equipment Company Limited	7,186	7,559
Shandong Zibo XinCat Pharmaceutical Company Limited	10,368	—
Total	<u>41,777</u>	<u>42,580</u>

Detailed list of joint companies investment:

Name of investees	Registration	Principal operations	Ratio	Vote right	Total of net assets at the end of this period	Total of operating income during this period	Profit after taxation during this period
Shandong Xinhua Longxin Chemical & Industrial Company Limited	Linzi Zone, Zibo City	Production and sales of Salicylic acid series (excluded dangerous and poisonous chemical)	40%	40%	28,076	56,653	1,051
Shandong Dadi Xinhua Chemical & Industrial Company Limited	Shouguang City	Production and sales of chemical products (excluded dangerous chemical)	49%	49%	26,327	12,838	327
Shandong Xinhua Changxing Chemical Equipment Company Limited	Zouping City	Production and sales of chemical facilities and fittings	35%	35%	21,124	5,189	(473)
Shandong Zibo XinCat Pharmaceutical Company Limited	Development Zone, Zibo City	Production preparations	20%	20%	25,957	94,453	3,018

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## 11. Fixed Assets

Item	Houses & Buildings	Machinery & Equipment	Transportation Equipment	Electronic Apparatus	Total
Original cost at beginning of year	486,525	1,097,378	18,025	27,342	1,629,270
Add: Increases in the year	18,832	49,191	743	1,112	69,878
Including: Construction-in-progress transferred in	555	1,354	—	—	1,909
Less: Decreases in the year	8,329	6,286	299	195	15,109
Cost at the end of the period	497,028	1,140,283	18,469	28,259	1,684,039
Accumulated depreciation at beginning of year	206,314	609,992	12,987	21,230	850,523
Add: Increases in the year	11,133	46,417	1,040	1,205	59,795
Less: Decrease in the year	4,486	2,907	273	174	7,840
Accumulated depreciation at the end of the period	212,961	653,502	13,754	22,261	902,478
Net value at 31 Dec 2006	280,211	487,386	5,038	6,112	778,747
Net value at 30 June 2007	284,067	486,781	4,715	5,998	781,561

No provision for impairment is made and there is no evidence indicating any impairment of fixed assets at the end of the period.

## 12. Construction-in-progress

Project	Beginning balance	Additions	Transfer to fixed assets	Other deduction	End balance	Source of funds	Project budget
Caffeine project	673	3,354	—	—	4,027	Self-owned	160,000
Xinhua (West) intel' building	4,628	—	—	—	4,628	—	—
Xinhua (East) intel' building	709	145	—	—	854	—	—
Injection GMP Revamping	16	1,475	—	—	1,491	Self-owned	80,000
Propyphenazone project	266	1,173	—	—	1,439	Self-owned	12,500
Calcium Polycarbophil project	188	106	—	—	294	Self-owned	6,000
Supply and marking warehouse renovation project	98	100	—	—	198	Self-owned	6,000
2005 DK production expansion	1,630	—	—	—	1,630	Self-owned	5,000
2005 high concentration waste water treatment shop renovation project	5,249	—	—	667	4,582	Self-owned	6,000
Repair workshop make up	3,496	141	—	—	3,637	Self-owned	4,000
Methyl Process of Theophylline Sodium Non-separation from Reaction Solution	3,450	2,363	—	—	5,813	Self-owned	3,000
Sewage treatment of Xinhua (East) intel' building	7,227	700	—	—	7,927	Self-owned	10,000
202 workshop Lidushen project	7,401	915	—	—	8,316	Self-owned	10,000
Research center of Xinhua (West) intel' building	—	1,178	—	—	1,178	—	40,000
Others	46,014	8,925	1909	—	53,030	Self-owned	—
Total	81,045	20,575	1909	667	99,044		

- 1) Interest capitalization does not apply to construction in progress because no specially-borrowed funds are used.
- 2) There is no impaired construction-in-progress at year-end, and thus no provision for impairment is made.

**13. Intangible Assets**

Item	Land use right	Software use right	Non-patented technology	Total
Amount at begin	106,091	2,655	6,550	115,296
Increase for this period	1,530	8	—	1,538
Decrease for this period	226	—	—	226
Amount at end	<u>107,395</u>	<u>2,663</u>	<u>6,550</u>	<u>116,608</u>
Accumulated amortization at 1 January 2007	17,059	1,438	3,497	21,994
Increase for this period	1,300	192	565	2,057
Decrease for this period	20	—	—	20
Accumulated amortization at 30 June 2007	<u>18,339</u>	<u>1,630</u>	<u>4,062</u>	<u>24,031</u>
Net value at 1 January 2007	<u>89,032</u>	<u>1,217</u>	<u>3,053</u>	<u>93,302</u>
Net value at 30 June 2007	<u>89,056</u>	<u>1,033</u>	<u>2,488</u>	<u>92,577</u>

There are no intangible assets impaired at year-end, and no provision for impairment is thus made.

**14. Deferred Tax Asset**

Item	2007.6.30	2006.12.31
Provision impairment	2,565	2,564
Inventories impairment	895	895
Financial assets available for sale	<u>4,500</u>	<u>4,500</u>
Total	<u>7,960</u>	<u>8,049</u>

**15. Short-term Loans**

Item	2007.6.30	2006.12.31	Annual interest rate (%)
Credit loans	48,718	55,234	HIBOR +1-1.2
Secured borrowing	<u>80,000</u>	<u>180,000</u>	5.508
Total	<u>128,718</u>	<u>235,234</u>	

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## 16. Notes Payable

Item	2007.6.30	2006.12.31
Bank acceptance	<u>178,079</u>	<u>97,067</u>

In the end balance, there are no notes payable due from shareholders who hold 5% and more of the Company's voting power.

## 17. Accounts Payable

Item	2007.6.30	2006.12.31
Accounts payable	<u>153,727</u>	<u>121,905</u>

- 1) There is RMB3,775,000 accounts payable aged over three years, most of which are unsettled payments for good in prior year.
- 2) In the end balance, there are no accounts payable due from shareholders who hold 5% and more of the Company's voting power.

## 18. Advances from Customers

Item	2007.6.30	2006.12.31
Advances from customers	<u>16,002</u>	<u>9,651</u>

- 1) Most of the advances from customers aged over one year are unsettled small residual payments.
- 2) In the end balance, there are no advances from customers due from shareholders who hold 5% and more of the Company's voting rights.

## 19. Staff Remuneration Payable

Item	Balance at 1 January 2007	Increase for this period	Decrease for this period	Balance at 30 June 2007
Wages	—	56,275	56,275	—
Benefit costs	15,297	—	4,601	10,696
Social insurance costs	—	14,450	14,450	—
Include: 1. medical insurance	—	2,201	2,201	—
2. pension insurance	—	10,551	10,551	—
3. unemploy insurance	—	925	925	—
4. injure insurance	—	454	454	—
5. fertility insurance	—	319	319	—
Accommodation scheme	328	6,795	6,669	454
Union funds	189	1,146	1,099	236
Education funds	12,456	852	338	12,970
Remuneration of the Directors and Supervisors	1,357	2,154	1,655	1,856
Others	2,121	8	2,129	—
Total	<u>31,748</u>	<u>81,680</u>	<u>87,216</u>	<u>26,212</u>

20. Taxes Payable

Item	2007.6.30	2006.12.31	Applicable
Income tax payable	5,129	3,320	15%, 33%
VAT payable	(7,094)	(3,009)	—
Sales tax payable	9	43	3%, 5%
Urban maintenance & construction tax payable	(407)	(867)	7%
Education surcharges payable	(146)	(371)	3%
Local education surcharges payable	35	56	1%
Payroll tax payable	75	122	—
Land-use tax payable	(2,001)	—	—
Property tax payable	4	15	1.2%
Land VAT payable	—	—	30%
Stamp tax payable	84	48	—
Total	<u>(4,312)</u>	<u>(643)</u>	

21. Dividends Payable

Item	2007.6.30	2006.12.31
State-owned shares	—	—
Legal person shares	—	—
Publicly held A-share	—	—
Publicly held H-share	3,000	—
Others	8,314	5,826
Total	<u>11,314</u>	<u>5,826</u>

22. Other Payables

Item	2007.6.30	2006.12.31
Other payables	<u>68,110</u>	<u>29,022</u>

- 1) The ending balance of other payables mainly includes the payment of construction, deposit of contracted workers, and etc.
- 2) In the end balance, there are no other payables due from the shareholders who hold 5% and more of the Company's voting rights.

## 23. Share Capital

Class of shares	2007.6.30 (share'000)	2006.12.31 (share'000)
1. Total number of conditional tradable shares	187,820	204,545
Stated-owned shares	163,259	163,259
Domestic legal person shares	—	16,720
Conditional tradable senior management A Shares	34	39
Others	24,527	24,527
2. Total number of unconditional tradable shares	269,493	252,768
Renminbi ordinary shares(A Shares)	119,493	102,768
Overseas listed foreign shares(H Shares)	150,000	150,000
3. Total number of shares	457,313	457,313

## 24 Capital Surplus

Item	2006.12.31	Additions	Deductions	2007.6.30
Upward revaluation of assets	60,910	—	—	60,910
Premium on stock	496,851	—	—	496,851
Receipt of donation	1,158	—	—	1,158
Others	—	67,892	—	67,892
Total	558,919	67,892	—	626,811

## 25. Surplus Reserves

Item	2006.12.31	Additions	Deductions	2007.6.30
Statutory surplus reserve	97,489	—	—	97,489
Discretionary surplus reserve	64,797	—	—	64,797
Total	162,286	—	—	162,286

## 26. Profit Distribution

Item	2007.6.30	2006.12.31
Net income	18,846	22,706
Add: Undistributed profit at beginning of the year	172,294	167,636
Profit available for the year	191,140	190,342
Less: Appropriation of statutory surplus reserve (10%)	—	2,078
Appropriation of statutory public welfare fund (5%)	—	—
Undistributed profit available for the year	191,140	188,264
Less: Appropriation of discretionary surplus reserve (10%)	—	—
Dividend payable on common stock	9,146	22,866
Undistributed profit at the end of the year	181,994	165,398
Including: Dividend in cash to be distributed	—	9,146
Add: Change in accounting policy	—	6,896

**27. Foreign Currency Statement Translation Difference**

Item	2007.6.30	2006.12.31
Foreign-currency statement translation difference	<u>697</u>	<u>708</u>

These results are from translating the EUR financial statements of Shandong Xinhua Pharmaceutical (European) GmbH (the overseas subsidiary of the Company) into RMB.

**28. Operating Income and Operating Cost**

Item	Operating income		Operating cost	
	2007.1-6	2006.1-6	2007.1-6	2006.1-6
Main operation	936,560	861,634	776,207	713,334
Other operating	<u>32,317</u>	<u>21,520</u>	<u>31,379</u>	<u>20,421</u>
Total	<u>968,877</u>	<u>883,154</u>	<u>807,586</u>	<u>733,755</u>

**The list of main operation**

Item	Revenue		Cost	
	2007.1-6	2006.1-6	2007.1-6	2006.1-6
Bulk pharmaceutical	595,240	502,943	484,687	403,064
Preparations	166,903	132,823	123,067	88,637
Medical Commercial Logistics	172,595	216,321	167,494	211,958
Chemical & other products	<u>1,822</u>	<u>9,547</u>	<u>959</u>	<u>9,675</u>
Total	<u>936,560</u>	<u>861,634</u>	<u>776,207</u>	<u>713,334</u>

**29. Taxes and Surcharges for Main Operations**

Item	2007.1-6	2006.1-6
Sales tax	38	64
City Construction Tax	3,268	2,605
Education surcharges	1,401	1,117
Cultural construction cost	<u>467</u>	<u>372</u>
Total	<u>5,174</u>	<u>4,158</u>

**30. Financial Expenses**

Item	2007.1-6	2006.1-6
Interest expenses	6,486	10,260
Less: Interest income	705	2,242
Exchange losses / gains	3,250	1,164
Banking charge	354	772
Others	<u>1,283</u>	<u>443</u>
Total	<u>10,668</u>	<u>10,397</u>

# FINANCIAL REPORT

(PREPARED UNDER PRC ACCOUNTING STANDARDS)

## 31. Assets Impairment

Item	2007.1-6	2006.1-6
Bad debts losses	5,808	—
Total	<u>5,808</u>	<u>—</u>

## 32. Fair Value Change Income/loss

Item	2007.1-6	2006.1-6
Derivative financial instruments income/loss	1,962	—
Total	<u>1,962</u>	<u>—</u>

## 33. Investment Income

Item	2007.1-6	2006.1-6
Held-to-maturity investments income	1,647	3,100
Financial assets available for sale income	167	—
Joint companies investments income	604	(713)
Others	(9)	—
Total	<u>2,409</u>	<u>2,387</u>

There are no major restrictions to recover the company's investment income.

## 34. Non-Operating Income

Item	2007.1-6	2006.1-6
Proceeds from disposal of fixed assets	10,621	480
Income from penalties	45	19
Others	400	—
Total	<u>11,066</u>	<u>499</u>

## 35. Non-Operating Expenses

Item	2007.1-6	2006.1-6
Loss from disposal of fixed assets	5,875	430
Overdue fines, penalties, excessive sewage discharge charges etc.	369	270
	34	—
Others	995	946
Total	<u>7,273</u>	<u>1,646</u>



**36. Income Tax**

Item	2007.1-6	2006.1-6
Income tax during this period	7,694	3,131
Deferred income tax	89	—
Total	<u>7,783</u>	<u>3,131</u>

**37. Cash Received Relating to Other Operating Activities**

Item	2007.1-6
Non-Operating income	420
Compensation	3,760
Other fund transactions	5,889
Total	<u>10,069</u>

**38. Cash Paid Relating to Other Operating Activities**

Item	2007.1-6
Travel expenses	1,886
Office expenses	1,239
Annual listing fee, audit fee and Board's fee	3,634
Sewage discharge fees	2,693
Entertainment expenses	912
Advertising, marketing expenses and sale services expenses	17,639
Freight charges	27,702
Technical development expenses	5,464
Others	18,649
Total	<u>79,818</u>

**7 NOTES TO THE FINANCIAL STATEMENTS OF THE COMPANY****1 Accounts Receivable**

Aging	2007.6.30	Bad Debts Ratio	Provision	2006.12.31	Bad Debts Ratio	Provision
Less than 1 year	323,485	86.72%	1,058	204,140	78.11%	933
1 to 2 years	33,954	9.10%	798	40,513	15.50%	2,381
2 to 3 years	13,064	3.50%	2,343	15,807	6.05%	7,959
Over 3 years	2,521	0.68%	529	886	0.34%	886
Total	<u>373,024</u>	<u>100.00%</u>	<u>4,728</u>	<u>261,346</u>	<u>100.00%</u>	<u>12,159</u>

In the end balance, there are no accounts receivable due from shareholders who hold 5% and more of the Company's voting rights.

## 2 Other Receivables

Aging	2007.6.30	Bad Debts Ratio	Provision	2006.12.31	Bad Debts Ratio	Provision
Less than 1 year	41,574	73.64%	471	27,211	46.88%	10
1 to 2 years	3,036	5.38%	—	18,790	32.37%	166
2 to 3 years	2,195	3.89%	—	2,306	3.97%	533
Over 3 years	9,647	17.09%	3,767	9,739	16.78%	3,529
Total	<u>56,452</u>	<u>100.00%</u>	<u>4,238</u>	<u>58,046</u>	<u>100.00%</u>	<u>4,238</u>

In the end balance, there are no accounts other receivables due from shareholders who hold 5% and more of the Company's voting rights.

## 3 Long-Term Equity Investments

Name of investees	2007.6.30	2006.12.31
Sino-USA Zibo Xinhua-Perrigo Pharmaceutical Company Limited	19,073	19,027
Shandong Xinhua Pharmaceutical (Europe) GmbH	1,995	1,995
Zibo Xinhua Drug Store Chain Company Limited	1,551	1,551
Zibo Xinhua Pharm. Design Institute Company Limited	304	304
Zibo Xinhua Sanhe Chemical & Industrial Company Limited	—	—
Shandong Xinhua Medicine Commerce Company Limited	47,738	47,738
Shandong Xinhua Longxin Chemical & Industrial Company Limited	11,115	10,694
Zibo Xinhua-Eastwest Pharmaceutical Company Limited	8,990	8,990
Shandong Dadi Xinhua Chemical & Industrial Company Limited	13,108	5,300
Shandong Xinhua Changxing Chemical Equipment Company Limited	7,186	7,559
Shandong Zibo XinCat Pharmaceutical Company Limited	10,368	—
Total	<u>121,428</u>	<u>103,158</u>

## 4. Operating Income and Operating Cost

Item	Operating income		Operating cost	
	2007.1-6	2006.1-6	2007.1-6	2006.1-6
Main operation	732,825	684,807	604,853	541,332
Other operating	30,173	19,372	31,139	20,421
Total	<u>762,998</u>	<u>704,179</u>	<u>635,992</u>	<u>561,753</u>

### The list of main operation

Item	Revenue		Cost	
	2007.1-6	2006.1-6	2007.1-6	2006.1-6
Bulk pharmaceutical	546,781	505,447	445,120	405,569
Preparations	184,958	143,257	158,771	99,071
Medical Commercial Logistics	3	27,868	3	27,017
Chemical & other products	1,083	8,235	959	9,675
Total	<u>732,825</u>	<u>684,807</u>	<u>604,853</u>	<u>541,332</u>

## 8. RELATED PARTY RELATIONSHIP AND TRANSACTIONS

### 1 Related Party Relationship

#### 1.1 Related Parties under a control relationship

Related Party Name	Place of registration	Main operations	Relation with the Company	Nature	Legal representative
Shadong Xinhua Pharmaceutical Group Company Limited	No. 14, East 1st Road, Zhangdian Dist., Zibo, Shandong Province.	Investment in the design of construction projects, property development and food and beverage, etc.	Immediate holding company of the Company	Wholly state-owned	Guo Qin
Shandong Hualu Holding Group Company Limited	No.1 Bangpeng Street, Jinan, Shandong Province.	Investment and management in fertilizer and petrochemicals, etc.	The ultimate holding company	Wholly state-owned	Li Tongdao

#### 1.2 Registered capital (and changes thereof) of related parties under a control relationship

Related Party Name	2006.12.31	Increase for the period	Decrease for the period	2007.6.30
Shadong Xinhua Pharmaceutical Group Company Limited	298,500	—	—	298,500
Shandong Hualu Holding Group Company Limited	800,000	—	—	800,000

#### 1.3 Shareholdings (and change thereof) of related parties under a control relationship

Related Party Name	Amount of shares		Ratio	2006.12.31
	2007.6.30	2006.12.31		
Shadong Xinhua Pharmaceutical Group Company Limited	163,259	163,259	35.70%	35.70%

## 1.4 Nature of related parties under no control relationships

### 1.4.1 Related parties controlled by the same holding shareholders

Related Party Name	Share ratio held by the holding company	Main business	Related Transactions with the Company
Shandong Xinhua Industry & Trade Company Limited	29.12%	Production and sale of chemical raw materials, etc.	Sale of power and waste materials, and purchase of raw materials
Zibo All-purpose Service Company Limited of Shandong Xinhua Pharmaceutical Group	100%	Kindergarten education, and etc.	Purchase of services and sale of power
Shandong Zibo XinCat Pharmaceutical Company Limited	80%	Production and sale of western medicine preparation, and chemical materials medicine and midway articles	Sale of power, leasing houses
Shandong Xinhua Bobang Chemical & Industrial Company Limited	53.55%	Production and sale of chemical production & materials, etc.	Purchase of materials
Shandong Xinhua Wanbo Chemical & Industrial Company Limited	90.63%	Production and sale of chemical production & materials, etc.	Purchase of materials, sale of power

### 1.4.2 Related parties as Affiliates and Joint Ventures

Related Party Name	Share ratio held by the Company	Main business	Related Transactions with the Company
Shandong Xinhua Longxin Chemical & Industrial Company Limited	40%	Production and sale of Salicylic acid product series	Purchase of materials
Shandong Dadi Xinhua Chemical & Industrial Company Limited	49%	Production and sale of chemicals	Purchase of materials
Shandong Xinhua Changxing Chemical Equipment Company Limited	35%	Production and sale of chemicals facilities and fittings	Purchase of glass-lined equipments

### 1.4.3 Related parties with other relationships

Related Party Name	The relationships with the Company	Main businesses	Related Transactions with the Company
Shandong Zibo Xinhua-Chemferm Pharmaceutical Company Limited	The same shareholder	Production and sale of cephal-product series	Sale of power and purchase of materials

## 2 Related Transactions

### 2.1 Sale of merchandise

Related Party Name	2007.1-6 Amount	2006.1-6 Amount	Remark
Shandong Xinhua Industry & Trade Company Limited	2,070	6,650	Sale of power and waste materials
Shandong Xinhua Wanbo Chemical & Industrial Company Limited	3,117	—	Sale of power and waste materials
Shandong Zibo XinCat Pharmaceutical Company Limited	657	411	Sale of power
Shandong Zibo Xinhua-Chemferm Pharmaceutical Company Limited	1,527	1,897	Sale of power
Zibo Packing & Decoration Company Limited of Shandong Xinhua Pharmaceutical Group	—	70	Sale of power
Zibo Xinhua-Perrigo Pharmaceutical Company Limited	—	1,285	Sale of power
Total	<u>7,371</u>	<u>10,313</u>	

The Company sells materials and waste materials to related parties at the market price and sells power at an agreed-upon price.

### 2.2 Purchase of materials

Related Party Name	2007.1-6 Amount	2006.1-6 Amount
Shandong Xinhua Industry & Trade Company Limited	1,900	4,933
Shandong Xinhua Wanbo Chemical & Industrial Company Limited	17,219	—
Zibo Packing & Decoration Company Limited of Shandong Xinhua Pharmaceutical Group	—	6,613
Shandong Zibo Xinhua-Chemferm Pharmaceutical Company Limited	17,161	4,731
Shandong Xinhua Bobang Chemical & Industrial Company Limited	4,669	4,967
Shandong Xinhua Longxin Chemical & Industrial Company Limited	330	2,723
Shandong Dadi Xinhua Chemical & Industrial Company Limited	14,141	—
Shandong Xinhua Changxing Chemical Equipment Company Limited	16	—
Zibo Xinhua-Perrigo Pharmaceutical Company Limited	—	1,388
Total	<u>55,436</u>	<u>25,355</u>

The Company purchase goods from the related parties at the market price.

# FINANCIAL REPORT

(PREPARED UNDER PRC ACCOUNTING STANDARDS)

## 2.3 Trademark using fee

Related Party Name	2007.1-6 Amount	2006.1-6 Amount
Shandong Xinhua Pharmaceutical Group Company Limited	1,100	1,000
Total	<u>1,100</u>	<u>1,000</u>

## 2.4 Lease-out Assets

Related Party Name	Nature of deal	2007.1-6 Amount	2006.1-6 Amount
Shandong Zibo XinCat Pharmaceutical Company Limited	House leasing	<u>300</u>	<u>700</u>
Total		<u>300</u>	<u>700</u>

The Company lets out assets to related parties at agree-upon price.

## 2.5 Lease-in Assets and Purchase-in Assets

Related Party Name	Nature of deal	2007.1-6 Amount	2006.1-6 Amount
Shandong Xinhua Pharmaceutical Group Company Limited	House and land leasing	500	—
Shandong Xinhua Pharmaceutical Group Company Limited	Purchase Assets	<u>—</u>	<u>1,499</u>
Total		<u>500</u>	<u>1,499</u>

## 2.6 Guarantee secured

On 28 September 2006, the Company signed an export bargainor credit contract with China Import & Export Bank for a contractual amount of RMB180,000,000 and for a period of 12 months. Shandong Hualu Holding Group Company Limited provided joint and several guarantee for the liabilities of the Company under the above contract. As at the end of 30 June 2007, the Company received RMB80,000,000 under the contract.

**3 Related Party Current Account Balances**

Related Party Name	A/C title	2007.6.30	2006.12.31
Shandong Xinhua Pharmaceutical Group Company Limited	Other payables	1,891	6
Shandong Zibo Xinhua-Chemferm Pharmaceutical Company Limited	Account payables	1,148	2,992
Zibo Packing & Decoration Company Limited of Shandong Xinhua Pharmaceutical Group	Account payables	1,652	1,470
Zibo All-purpose Service Company Limited of Shandong Xinhua Pharmaceutical Group	Other receivables	—	1,374
Shandong Xinhua Changxing Chemical Equipment Company Limited	Other receivables	486	26
Shandong Xinhua Changxing Chemical Equipment Company Limited	Account receivable	2,984	6,467
Shandong Xinhua Industry & Trade Company Limited	Account receivable	40,676	40,668
Shandong Xinhua Industry & Trade Company Limited	Account payables	—	1,371
Shandong Xinhua Industry & Trade Company Limited	Other payables	—	273
Shandong Zibo Xinhua-Chemferm Pharmaceutical Company Limited	Notes payable	12,700	600
Shandong Xinhua Bobang Chemical & Industrial Company Limited	Account payables	1,813	598
Shandong Xinhua Bobang Chemical & Industrial Company Limited	Notes payable	624	330
Shandong Xinhua Longxin Chemical & Industrial Company Limited	Advances to suppliers	2,243	2,123
Shandong Zibo XinCat Pharmaceutical Company Limited	Account receivable	8,459	8,048
Shandong Xinhua Wanbo Chemical & Industrial Company Limited	Advances from customers	—	4
Shandong Xinhua Wanbo Chemical & Industrial Company Limited	Advances to suppliers	8,450	2,959
Shandong Xinhua Wanbo Chemical & Industrial Company Limited	Notes payable	700	—
Shandong Dadi Xinhua Chemical & Industrial Company Limited	Notes payable	2,050	—

**9. CONTINGENCIES**

None

**10. POST BALANCE SHEET DATE EVENTS**

The Company has no significant subsequent events to be disclosed.

**11. SUPPLEMENTARY INFORMATION**
**1 The reconciliation table of transitional adjustments in profit after taxation from differences during this period**

Item	Amount
Profit after taxation during 2006.1.1-2006.6.30 (under the original ASBE)	12,362
Add: Total of affects from retrospective adjustments	(83)
Include: Operating cost	10,658
Selling expenses	—
Administrative expenses	(10,658)
Fair value change income	—
Investment income	—
Taxation	—
Others	(83)
Less: Minority shareholders' equity of affects from retrospective adjustments	—
Profit attributable to the equity shareholders of the Parent during 2006.1.1-2006.6.30 (under the current ASBE)	12,279

**2. Statement of provision**

Item	Beginning balance	Retaining	Deductions Reversal	Resell	Ending balance
1. Bad debts provided	15,467	5,808	(329)	313	21,290
2. Inventory write-down provided	7,136	—	—	407	6,729
3. Provided for impairment of financial assets available for sale	—	—	—	—	—
4. Provided for impairment of held-to-maturity investments	—	—	—	—	—
5. Provided for impairment of long-term equity investment	—	—	—	—	—
6. Provided for impairment of investment property	—	—	—	—	—
7. Provided for impairment of fixed assets	—	—	—	—	—
8. Provided for impairment of construction materials	—	—	—	—	—
9. Provided for impairment of construction in progress	—	—	—	—	—
10. Provided for impairment of biological assets for production	—	—	—	—	—
Include: Provided for impairment of mature biological assets for production	—	—	—	—	—
11. Provided for impairment of fuel assets	—	—	—	—	—
12. Provided for impairment of intangible assets	—	—	—	—	—
13. Provided for impairment of goodwill	—	—	—	—	—
14. Others	—	—	—	—	—
Total	22,603	5,808	(329)	720	28,019



3. Profit and loss adjusted account

(2006.1.1-6.30)

Item	Before adjusted	After adjusted
Operating cost	723,097	733,755
Selling expenses	74,963	74,963
Administrative expenses	56,434	45,776
Fair value change income	—	—
Investment income	2,387	2,387
Profit after taxation	12,362	12,279

4 Rate of return on equity and earnings per share

Item	Rate of return on equity				EPS (RMB)			
	Fully diluted		Weighted average		Basic		Diluted	
	2007.1-6	2006.1-6	2007.1-6	2006.1-6	2007.1-6	2006.1-6	2007.1-6	2006.1-6
Profit attributable to the equity shareholders of the Parent	1.32%	0.92%	1.37%	0.91%	0.041	0.027	0.041	0.027
Profit attributable to the equity shareholders of the Parent (excluding extraordinary items)	0.98%	0.81%	1.02%	0.80%	0.031	0.024	0.031	0.024

5 Non-routine profit or loss

Item	2007.1-6		2006.1-6	
	Before income tax	After income tax	Before income tax	After income tax
Held-to-maturity investments profit/loss	1,647	1,400	3,100	2,276
Profit/loss from the disposal of non-current assets	4,747	4,035	50	37
Net amount of other non-operating income and expenses	(955)	(871)	(1,196)	(950)
Other extraordinary items	329	279	48	35
Total	<u>5,768</u>	<u>4,843</u>	<u>2,002</u>	<u>1,398</u>

# FINANCIAL REPORT

(PREPARED UNDER HONG KONG GENERALLY ACCEPTED ACCOUNTING PRINCIPLES)

## CONDENSED CONSOLIDATED INCOME STATEMENT

		(unaudited) For the six months ended 30th June 2007 RMB'000	(unaudited) For the six months ended 30th June 2006 RMB'000
	NOTES		
Turnover	3	977,688	869,353
Cost of sales		(812,985)	(707,045)
Gross profit		164,703	162,308
Other operating income		9,662	6,857
Selling expenses	4	(72,418)	(82,682)
Administrative expenses	4	(63,263)	(57,915)
Other operating expenses	4	(1,398)	(1,646)
Share of results of associates		604	(713)
Finance costs		(7,769)	(10,704)
Profit before taxation		30,121	15,505
Income tax expense	5	(7,783)	(3,131)
Profit for the period		22,338	12,374
Attributable to :			
Equity holders of the Company		19,144	12,439
Minority interests		3,194	(65)
		22,338	12,374
Earnings per share — basic	6	RMB0.042	RMB0.027
Interim dividend	7	—	—

**CONDENSED CONSOLIDATED BALANCE SHEET**

		(unaudited) At 30th June 2007 RMB'000	(audited) At 31st December 2006 RMB'000
	NOTES		
<b>Non-current assets</b>			
Technical know-how	8	2,488	3,052
Property, plant and equipment	8	785,712	779,316
Construction-in-progress	8	103,807	85,922
Prepaid lease payments on land use rights	8	86,608	86,404
Interests in associates		41,777	42,580
Available-for-sale investments		24,425	23,777
		<u>1,044,817</u>	<u>1,021,051</u>
<b>Current assets</b>			
Inventories		222,163	224,356
Trade and bills receivables	9	324,408	233,499
Prepaid lease payments on land use rights	8	2,448	2,419
Other receivables, deposits and prepayment		79,079	49,647
Amount due from immediate holding company		28,598	46,874
Amounts due from associates		14,172	19,861
Available-for-sale investments		—	117,000
Pledged bank deposits		57,000	29,401
Derivative financial instruments		2,095	134
Bank balances and cash		181,890	133,134
		<u>911,853</u>	<u>856,325</u>
Assets classified as held for sale		—	4,199
		<u>911,853</u>	<u>860,524</u>
<b>Current liabilities</b>			
Trade and bills payables	10	311,119	213,080
Other payables and accrued charges		100,730	53,267
Amount due to an associate		2,050	—
Tax payable		5,129	3,320
Unsecured short-term bank loans	11	128,718	235,234
		<u>547,746</u>	<u>504,901</u>
<b>Net current assets</b>		<u>364,107</u>	<u>355,623</u>
<b>Total assets less current liabilities</b>		<u>1,408,924</u>	<u>1,376,674</u>
<b>Capital and reserves</b>			
Share capital	12	457,313	457,313
Reserves		921,818	902,685
Proposed final dividend		—	9,146
<b>Equity attributable to equity holders of the Company</b>		<u>1,379,131</u>	<u>1,369,144</u>
<b>Minority interests</b>		<u>25,517</u>	<u>3,343</u>
<b>Total equity</b>		<u>1,404,648</u>	<u>1,372,487</u>
<b>Non-current liability</b>			
Deferred tax liabilities		4,276	4,187
		<u>1,408,924</u>	<u>1,376,674</u>

# FINANCIAL REPORT

(PREPARED UNDER HONG KONG GENERALLY ACCEPTED ACCOUNTING PRINCIPLES)

## CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

(unaudited)  
Attributable to equity holders of the Company

	Share capital RMB'000	Share premium RMB'000	Capital reserve RMB'000	Reserve funds RMB'000	Asset revaluation reserve RMB'000	Exchange reserve RMB'000	Retained earnings RMB'000	Dividend reserve RMB'000	Total RMB'000	Minority interests RMB'000	Total RMB'000
At 1st January 2006	457,313	466,618	78,642	160,326	25,850	444	156,986	22,866	1,369,045	1,092	1,370,137
2005 final dividend paid	—	—	—	—	—	—	—	(22,866)	(22,866)	—	(22,866)
Exchange difference arising on translation of overseas operation	—	—	—	—	—	212	—	—	212	—	212
Profit (loss) for the period	—	—	—	—	—	—	12,439	—	12,439	(65)	12,374
Capital contribution by minority shareholder of a subsidiary	—	—	—	—	—	—	—	—	—	3,003	3,003
At 30th June 2006	<u>457,313</u>	<u>466,618</u>	<u>78,642</u>	<u>160,326</u>	<u>25,850</u>	<u>656</u>	<u>169,425</u>	<u>—</u>	<u>1,358,830</u>	<u>4,030</u>	<u>1,362,860</u>
At 1st January 2007	457,313	466,618	78,642	162,404	25,850	648	168,523	9,146	1,369,144	3,343	1,372,487
2006 final dividend paid	—	—	—	—	—	—	—	(9,146)	(9,146)	—	(9,146)
Exchange difference arising on translation of overseas operation	—	—	—	—	—	(11)	—	—	(11)	(9)	(20)
Profit (loss) for the period	—	—	—	—	—	—	19,144	—	19,144	3,194	22,338
Acquisition of a subsidiary	—	—	—	—	—	—	—	—	—	18,989	18,989
At 30th June 2007	<u>457,313</u>	<u>466,618</u>	<u>78,642</u>	<u>162,404</u>	<u>25,850</u>	<u>637</u>	<u>187,667</u>	<u>—</u>	<u>1,379,131</u>	<u>25,517</u>	<u>1,404,648</u>

**CONDENSED CONSOLIDATED CASH FLOW STATEMENT**

	(unaudited) For the six months ended 30th June 2007 <i>RMB'000</i>	(unaudited) For the six months ended 30th June 2006 <i>RMB'000</i>
Net cash from operating activities	126,271	4,929
Net cash from (used in) investing activities	45,916	(29,336)
Net cash used in financing activities	(123,431)	(97,311)
Increase (decrease) in cash and cash equivalents	48,756	(121,718)
Cash and cash equivalents at 1st January	133,134	298,042
Cash and cash equivalents at 30th June, represented by bank balances and cash	<u>181,890</u>	<u>176,324</u>

**NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS****1. BASIS OF PREPARATION AND PRINCIPAL ACCOUNTING POLICIES**

The unaudited condensed consolidated interim financial statements have been prepared in accordance with the applicable disclosure requirements set out in Appendix 16 to the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (“Listing Rules”) and with the Hong Kong Accounting Standard (“HKAS”) No.34 “Interim Financial Reporting” which is one of the Hong Kong Financial Reporting Standards (“HKFRSs”) issued by the Hong Kong Institute of Certified Public Accountants (“HKICPA”).

The condensed consolidated interim financial statements have been prepared under the historical costs basis except for property, plant and equipment and financial instruments, which are measured at fair values or revalued amounts, as appropriate.

The accounting policies used in the condensed consolidated interim financial statements are consistent with those followed in the preparation of the annual financial statements of the Company and its subsidiaries (the “Group”) for the year ended 31st December 2006, except as described below.

In the current interim period, the Group has applied, for the first time, a number of new standards, amendment and interpretations (collectively referred to as “new HKFRSs”) issued by the HKICPA, which are effective for accounting periods beginning on or after 1st December 2005, 1st January 2006, 1st March 2006, 1st May 2006, 1st June 2006, 1st November 2006 and 1st January 2007. The adoption of the new HKFRSs has had no material effect on how the results and financial position for the current or prior accounting periods have been prepared and presented. Accordingly, no prior period adjustment has been required.

**2. SUMMARY OF THE EFFECTS OF THE CHANGES IN ACCOUNTING POLICIES**

The Group has not early applied the following new standards, amendment, interpretations that have been issued but are not yet effective. The directors of the Company anticipate that the application of these standards, amendment or interpretations, will have no material impact on how the results and financial position of the Group are prepared and presented.

HKAS 23 (Revised)	Borrowing Cost <sup>1</sup>
HKFRS 8	Operating Segments <sup>1</sup>
HK(IFRIC)-Int-11	HKFRS2-Group and Treasury Share Transactions <sup>2</sup>
HK(IFRIC)-Int-12	Service Concession Arrangements <sup>3</sup>

<sup>1</sup> Effective for annual periods beginning on or after 1st January 2009

<sup>2</sup> Effective for annual periods beginning on or after 1st March 2007.

<sup>3</sup> Effective for annual periods beginning on or after 1st January 2008.

### 3. SEGMENT INFORMATION

The Group is principally engaged in the development, production and sales of pharmaceutical products, preparations, chemicals and other products. Its major place of operation is in the Peoples' Republic of China (the "PRC").

(i) By business segments :

	(unaudited) For the six months ended 30th June 2007			(unaudited) For the six months ended 30th June 2006		
	Pharmaceutical business RMB'000	Other operations RMB'000	Total RMB'000	Pharmaceutical business RMB'000	Other operations RMB'000	Total RMB'000
Segment revenues	983,584	3,766	987,350	866,203	3,150	869,353
Segment results	33,520	3,766	37,286	23,772	3,150	26,922
Share of results of associates			604			(713)
Finance costs			(7,769)			(10,704)
Profit before taxation			30,121			15,505
Income tax expense			(7,783)			(3,131)
Profit for the period			22,338			12,374
Capital expenditure	43,093	—	43,093	43,130	—	43,130
Depreciation and amortisation	61,286	—	61,286	51,326	—	51,326
Amortisation of technical know-how	564	—	564	564	—	564

	(unaudited) As at 30th June 2007			(unaudited) As at 31st December 2006		
	Pharmaceutical business RMB'000	Other operations RMB'000	Total RMB'000	Pharmaceutical business RMB'000	Other operations RMB'000	Total RMB'000
Assets						
Segment assets	1,890,468	24,425	1,914,893	1,698,218	140,777	1,838,995
Interests in associates	41,777	—	41,777	42,580	—	42,580
Total assets			1,956,670			1,881,575
Liabilities						
Segment liabilities	(542,617)	—	(542,617)	(501,581)	—	(501,581)
Unallocated liabilities	—	—	(9,405)	—	—	(7,507)
Total liabilities			(552,022)			(509,088)

# FINANCIAL REPORT

(PREPARED UNDER HONG KONG GENERALLY ACCEPTED ACCOUNTING PRINCIPLES)

(ii) By geographical location of customers :

	(unaudited)	
	Segment revenues	
	Six months ended	Six months ended
	30th June 2007	30th June 2006
	RMB'000	RMB'000
PRC (including Hong Kong)	557,860	516,260
Europe	139,417	130,971
Americas	150,953	169,326
Others	129,458	52,796
	<u>977,688</u>	<u>869,353</u>

## 4. EXPENSES

Expenses (income) included in selling expense, administrative expenses and other operating expenses are analysed as follows:

	(unaudited)	(unaudited)
	Six months ended	Six months ended
	30th June 2007	30th June 2006
	RMB'000	RMB'000
Depreciation	60,062	50,114
Amortisation of prepaid lease payments on land use rights	1,224	1,212
Amortisation of technical know-how	564	564
Staff costs (excluding emoluments of directors and supervisors)	79,526	60,297
Contributions to retirement scheme for the staff	10,551	9,181
Gain on disposal of property, plant and equipment	<u>(4,747)</u>	<u>(50)</u>

## 5. INCOME TAX EXPENSE

The amount of tax charged to the condensed consolidated income statement represents :

	(unaudited)	(unaudited)
	Six months ended	Six months ended
	30th June 2007	30th June 2006
	RMB'000	RMB'000
Current period PRC enterprise income tax	7,694	3,131
Deferred taxation	<u>89</u>	<u>—</u>
	<u>7,783</u>	<u>3,131</u>

(a) PRC enterprise income tax is calculated at the applicable rates in accordance with the relevant laws and regulations in the PRC.



- (b) The Company and a subsidiary are located in the high-technology economic zone of Zibo City and are entitled to preferential PRC enterprise income tax rate of 15% from year 2002 onwards, according to [1994] Guo Shui Fa No.151 "The notice of applying favourable tax policies for the new and high technology companies" issued by the State Administration of Taxation. The companies have obtained the relevant approvals from the local tax bureau. From year 2004 onwards, the operating results of the companies derived from business conducted in the high-technology economic zone are subject to a preferential income tax rate of 15% while the business conducted outside the high-technology economic zone are subject to an income tax rate of 33%. This has been filed with the local tax bureau as a record.

Other companies within the Group are subject to income tax rate at 33% on their taxable income for the six months ended 30th June 2006 and 2007 except SINO-USA Zibo Xinhua-Perrigo Pharmaceutical Company Limited is subject to income tax rate at 24%.

- (c) No provision for Hong Kong Profits Tax has been made as the Group's income neither arises in, nor is derived from, Hong Kong for the six months ended 30th June 2007 and 2006.

## 6. EARNINGS PER SHARE - BASIC

The calculation of basic earnings per share is based on the Group's profit attributable to equity holders of the Company of RMB19,144,000 (2006 : RMB12,439,000) and based on the weighted average of 457,312,830 shares (2006 : 457,312,830 shares) in issue during the period.

There was no dilution effect on the basic earnings per share for the six months ended 30th June 2007 and 2006 as there were no dilutive shares outstanding during the six months ended 30th June 2007 and 2006.

## 7. INTERIM DIVIDEND

The board of the directors of the Company did not recommend the payment of an interim dividend for the six months ended 30th June 2007 (2006 : Nil).

## 8. CAPITAL EXPENDITURES

	Prepaid lease payments on land use rights RMB'000	Technical know-how RMB'000	(unaudited) Property, plant and equipment RMB'000	Construction- in-progress RMB'000	Total RMB'000
Net carrying values at 1st January 2007	88,823	3,052	779,316	85,922	957,113
Additions	330	—	22,857	19,906	43,093
Disposals	—	—	(3,425)	(114)	(3,539)
Transfers	—	—	1,910	(1,910)	—
Acquisition of a subsidiary	1,127	—	45,116	3	46,246
Depreciation and amortisation	(1,224)	(564)	(60,062)	—	(61,850)
Net carrying values at 30th June 2007	<u>89,056</u>	<u>2,488</u>	<u>785,712</u>	<u>103,807</u>	<u>981,063</u>
Representing:					
Non-current portion	<u>86,608</u>	<u>2,488</u>	<u>785,712</u>	<u>103,807</u>	<u>978,615</u>
Current portion	<u>2,448</u>	<u>—</u>	<u>—</u>	<u>—</u>	<u>2,448</u>

## 9. TRADE AND BILLS RECEIVABLES

At 30th June 2007, the aging analysis of the trade and bills receivables, net of allowances is as follows :

	(unaudited) At 30th June 2007 RMB'000	(audited) At 31st December 2006 RMB'000
Within one year	270,179	186,017
More than one year but less than two years	37,592	39,584
More than two years but less than three years	16,637	7,898
	<u>324,408</u>	<u>233,499</u>

The Group's turnover from export sales is on letter of credit or documents against payment. The remaining balances of turnover are on open account terms which are partially covered by customers' stand-by letter of credit or bank guarantees.

## 10. TRADE AND BILLS PAYABLES

At 30th June 2007, the aging analysis of the trade and bills payables is as follows :

	(unaudited) At 30th June 2007 RMB'000	(audited) At 31st December 2006 RMB'000
Within one year	302,919	198,906
More than one year but less than two years	1,767	10,388
More than two years but less than three years	2,658	428
Over three years	3,775	3,358
	<u>311,119</u>	<u>213,080</u>

## 11. UNSECURED SHORT-TERM BANK LOANS

	(unaudited) At 30th June 2007 RMB'000	(audited) At 31st December 2006 RMB'000
Unsecured bank loans due within one year	<u>128,718</u>	<u>235,234</u>

**12. SHARE CAPITAL**

	(unaudited) At 30th June 2007		(audited) At 31st December 2006	
	Number of shares'000	RMB'000	Number of shares'000	RMB'000
<b>Issued and fully paid:</b>				
<b>State-owned legal person shares of RMB 1 each</b>				
At the beginning of the period / year	163,259	163,259	214,440	214,440
Decrease as a result of State-owned Share Reform (Note 1)	—	—	(26,654)	(26,654)
Transferred to PRC legal person shares (Note 2)	—	—	(24,527)	(24,527)
At the end of period / year	163,259	163,259	163,259	163,259
<b>Promoters' shares of RMB 1 each</b>				
At the beginning of the period / year	16,720	16,720	16,720	16,720
Transferred to A shares	(16,720)	(16,720)	—	—
At the end of period / year	—	—	16,720	16,720
<b>PRC legal person shares of RMB 1 each</b>				
At the beginning of the period / year	24,527	24,527	—	—
Transferred from state-owned shares (Note 2)	—	—	24,527	24,527
At the end of period / year	24,527	24,527	24,527	24,527
<b>Senior officers' shares of RMB 1 each</b>				
At the beginning of the period / year	39	39	44	44
Decrease as a result of senior management terminated	—	—	(5)	(5)
Decrease as a result of shares sold from senior management	(5)	(5)	—	—
At the end of period / year	34	34	39	39
<b>A shares of RMB 1 each</b>				
At the beginning of the period / year	102,768	102,768	76,109	76,109
Increase as a result of State-owned Share Reform (Note 1)	—	—	26,659	26,659
Transferred from promoter and senior management	16,725	16,725	—	—
At the end of period / year	119,493	119,493	102,768	102,768
<b>H shares of RMB 1 each</b>				
At the beginning and the end of the period / year	150,000	150,000	150,000	150,000
	<u>457,313</u>	<u>457,313</u>	<u>457,313</u>	<u>457,313</u>

Notes :

1. In accordance with the revised share reform of the Company for the conversion of non-tradable A shares to tradable A shares ("Revised Share Reform"), the holders of the non-tradable A shares, Shandong Xinhua Pharmaceutical Group Company Limited ("SXPGC"), which was also an immediate holding company of the Company, offered as consideration, 3.5 shares of non-tradable A shares of the Company for every 10 tradable A shares held by A share shareholders as registered on the registration date in respect of the implementation of the Revised Share Reform. Upon the completion of the reform, SXPGC offered 26,653,665 non-tradable A shares as condition to have trading right in the A share market. These shares rank *pari passu* in all respects with other shares in issue.
2. On 27th November 2006, the Company received a notice from SXPGC that shares held by SXPGC in the Company have been subject to judicial sale, judicial freezing and pledging. The said judicial sale, judicial freezing and pledging of shares held by SXPGC in the Company is due to various loans to SXPGC and guarantees given by SXPGC for its own benefits and the benefits of its subsidiaries and third parties, and financial disputes involving SXPGC and SXPGC subsidiaries (but excluding the Company and its subsidiaries). As a result, a total of 24,527,000 shares held by SXPGC in the Company have been sold via judicial auction, and the total shares held by SXPGC in the Company before and after the said sale has decreased from 187,786,000 shares (representing 41.06% of the total share capital of the Company) to 163,259,000 shares (representing 35.70% of the total share capital of the Company).

## 13. CAPITAL COMMITMENTS

- (i) At 30th June 2007, the Group had the following capital commitments principally related to construction-in-progress and purchase of property, plant and equipment in respect of buildings and production facilities which were not provided for in the condensed consolidated financial statements:

	(unaudited) At 30th June 2007 RMB'000	(audited) At 31st December 2006 RMB'000
Contracted but not provided for	20,678	15,621
Authorised but not contracted for	143,270	143,270
	<u>163,948</u>	<u>158,891</u>

- (ii) Other commitments

The Group had capital commitment contracted but not provided for totalling RMB7,440,000 in respect of investment in an associate with 49% equity interest as at 31st December 2006. The capital commitment had been injected into the associate during the 2007 interim period. The associate is engaged in production and sale of chemical products in the PRC.

**14. RELATED PARTY TRANSACTIONS**

Significant related party transactions, which were carried out in the normal course of the Group's business are as follows :

	(unaudited) Six months ended 30th June 2007 RMB'000	(unaudited) Six months ended 30th June 2006 RMB'000
SXPGC and its subsidiaries		
— Sale of water, electricity and steam and raw materials	6,714	9,028
— Purchase of raw materials	40,948	21,244
— Rental income	—	700
— Rental expense	500	—
— Purchase of machineries	—	1,499
— Payment of annual trademark license fee	1,100	1,000
Associates		
— Sale of water, electricity and steam	657	1,285
— Rental income	300	—
— Purchase of raw materials	14,488	4,111
— Interest income received	—	135
	<u>          </u>	<u>          </u>

Note:

On 7th December 1996, the Group was granted the exclusive right to use the trademark "Xinhua" ("Trademark") by SXPGC for its existing and future products in and outside the PRC at an initial annual fee of RMB600,000 increasing at the rate of an extra RMB100,000 per year until the annual fee reaches the cap amount of RMB1,100,000, which shall stay as such until the agreement is terminated. The terms of the agreement shall continue to have effect during the validity period of the Trademark, being 28th February 2013, subject to further renewal of the registration of the Trademark. During the period ended 30th June 2007, the annual fee paid by the Group was RMB1,100,000 (2006 : RMB1,000,000).

**15. CONTINGENT LIABILITIES**

The Group has no significant contingent liabilities for the six months ended 30th June 2007.

**16. EVENTS AFTER BALANCE SHEET DATE**

Up to the date of this report, the Group has no significant events after balance sheet date.

### (1) DOCUMENTS FOR INSPECTION

1. The original copy of the Company's 2006 Interim Report signed by the Chairman of the Board.
2. Financial statements for the six months ended 30 June 2006 signed by the Chairman of the Board, the financial controller and the chief of accounting department of the Company.

### (2) PLACE FOR INSPECTION

Office of the Secretary to the Board of the Company.

As at the date of this Report, the Board consists of the following directors:

Ms. Guo Qin;  
Mr. Liu Zhenwen;  
Mr. Ren Fulong;  
Mr. Zhao Songguo;

and the following independent non-executive directors:

Mr. Dai Qingjun;  
Mr. Mok Chung Kwan, Stephen;  
Mr. Xu Guojun;  
Mr. Sun Minggao