China Shineway Pharmaceutical Group Limited

中國神威藥業集團有限公司

(incorporated in the Cayman Islands with limited liability)

Stock Code : 2877

Leading Modern
CHINESE MEDICINE

ANNUAL REPORT 2007

Content

Corporate Information

BOARD OF DIRECTORS

Executive Directors

Mr. Li Zhenjiang *(Chairman of the Board)*
Ms. Wang Zhihua
Ms. Xin Yunxia
Mr. Li Huimin
Mr. Hung, Randy King Kuen

Independent Non-executive Directors

Mr. Ren Dequan
Mr. Li Kung Man
Ms. Cheng Li

Audit Committee

Mr. Li Kung Man *(Committee Chairman)*
Mr. Ren Dequan
Ms. Cheng Li

Remuneration Committee

Ms. Cheng Li *(Committee Chairman)*
Mr. Li Kung Man
Ms. Xin Yunxia

AUTHORIZED REPRESENTATIVES

Ms. Wang Zhihua
Mr. Li Huimin

QUALIFIED ACCOUNTANT

Ms. Wong Mei Shan

COMPANY SECRETARY

Ms. Wong Mei Shan

AUDITORS

Deloitte Touche Tohmatsu

REGISTERED OFFICE

Cricket Square, Hutchins Drive
P.O. Box 2681, Grand Cayman KY1-1111
Cayman Islands

HEAD OFFICE

Luan Cheng, Shijiazhuang
Hebei Province, The PRC

PRINCIPAL PLACE OF BUSINESS IN HONG KONG

Suite 5201, 52/F., Central Plaza
18 Harbour Road, Wanchai, Hong Kong

PRINCIPAL SHARE REGISTRAR AND TRANSFER OFFICE

Butterfield Fund Services (Cayman) Limited
Butterfield House, 68 Fort Street
P.O. Box 705, George Town
Grand Cayman, Cayman Islands

HONG KONG BRANCH SHARE REGISTRAR AND TRANSFER OFFICE

Computershare Hong Kong Investor Services Limited
Shops 1712-1716
17th Floor, Hopewell Centre
183 Queen's Road East
Wanchai
Hong Kong

PRINCIPAL BANKERS

The Bank of East Asia, Limited

The Hongkong and Shanghai Banking Corporation Limited

Bank of China, Zhong Shan Branch
Shijiazhuang, Hebei Province

Bank of China, Lang Fang Branch
Lang Fang City, Hebei Province

LEGAL ADVISERS

As to Hong Kong Law
Woo Kwan Lee & Lo

As to Cayman Islands Law
Conyers Dill & Pearman, Cayman

STOCK CODE

2877 (listed on the Main Board of The Stock Exchange of Hong Kong Limited)

WEBSITES

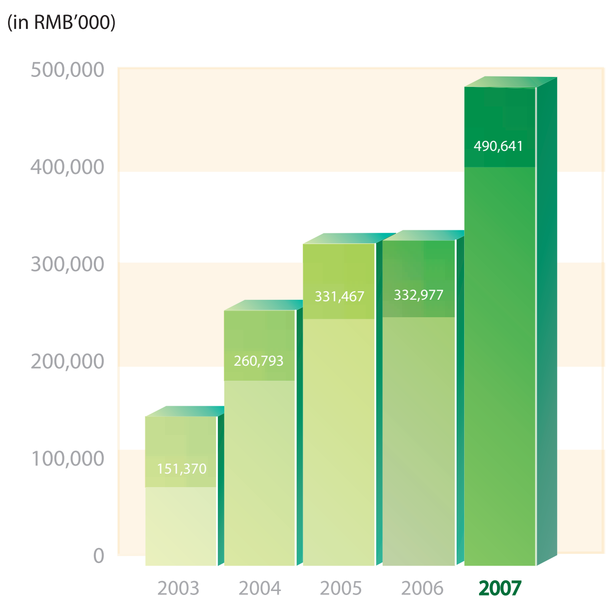
www.shineway.com.hk
www.irasia.com/listco/hk/shineway

FINANCIAL SUMMARY

(in RMB'000)

	2003	2004	2005	2006	**2007**
RESULTS					
Turnover	604,042	703,575	831,379	841,475	**1,012,885**
Gross profit	289,040	451,577	556,607	592,300	**738,038**
Profit before taxation	185,082	280,809	342,452	387,034	**575,941**
Profit attributable to shareholders	151,370	260,793	331,467	332,977	**490,641**
Basic earnings per share	RMB0.25	RMB0.42	RMB0.40	RMB0.40	**RMB0.59**
Dividends	0	0	181,940	181,940	**314,260**
ASSETS AND LIABILITIES					
Total assets	631,062	1,570,413	1,845,248	2,007,743	**2,408,737**
Total liabilities	(171,437)	(134,144)	(215,000)	(238,490)	**(339,462)**
Minority interests	(63,889)	(23,542)	0	0	**0**
Shareholders' equity	395,736	1,412,727	1,630,248	1,769,253	**2,069,275**

PROFIT ATTRIBUTABLE TO SHAREHOLDERS



GROSS AND NET PROFIT MARGINS

Major Achievements and Awards

Major Achievements and Awards of China Shineway in 2007

January

- The Shineway brand Qing Kai Ling injection and Jiangzhi Tongluo soft capsule have been included in the "China High-Tech Products Catalog"

- The SHINEWAY brand was selected as one of the "China Top 500 Most Valuable Trademarks" by China Brand Research Institute

- The Shineway brand of Shen Mai injection and Qing Kai Ling injection were named as "Most Valuable Hi-Tech Product"

February

- Qing Kai Ling injection, Guan Xin Ning injection and Dengzhan Huasu injection under the Shineway brand, have been labeled as "Good Quality/Good Price" by the National Development and Reformation Committee

March

- China Shineway was named by the China Quality Association for Pharmaceuticals as first batch of thirteen "Model Enterprise of Quality & Integrity in China Pharmaceutical Industry"

April

- China Shineway was included as "Top 100 Companies in China Pharmaceutical Industry of 2006"

- A new medicine and its production know-how for treatment of chronic nephritis developed by China Shineway received an invention patent certificate issued by the Intellectual Property Office of the PRC

- Promulgated by the Science and Technology Department of Hebei Province, China Shineway was honored as Hebei Province High-Tech Enterprise again, and seven products under the Shineway brand are also being included in the first group of Hebei Province High-Tech Products

Major Achievements and Awards

May

- China Shineway received two more invention patents issued by the Intellectual Property Office of the PRC for an application of total triterpenes of centella asiaticain and a modernized Chinese medicine for treatment of prostatic hyperlasis

June

- A health food certificate was awarded by the State Food and Drug Administration of PRC, for Dan Ge Shu Xin Soft Capsule

July

- Chairman Li Zhenjiang was appointed as the Honorary Council Member of the Chinese Medicine Society

- Ao Sha En Injection, a new product being developed by China Shineway was chosen to be included in the 2007 Hebei Province Science and Technology Research and Development Project

- China Shineway received another invention patent of "a medicine compound and its preparation method for preventing and controlling damage caused by cerebral ischemia"

August

- Applications of five Shineway products registration were accepted by the Canadian health authorities

- The construction of Shineway Modern Technology and Quality Center was completed

- The Ministry of Labor and Social Security, All China Federation of Trade Unions and the China Enterprise Federation jointly honored China Shineway as one of the "Model Enterprise in Harmonious Labor Relations"

Major Achievements and Awards

September

- Shineway Yishen Jianyao Oral Liquid received patent sponsorship from Shijiazhuang Intellectual Property Office

October

- At the "4th China Human Resources Management Annual Ceremony", China Shineway received the award of "2007 Best Employer in China" and Chairman Li Zhenjiang, was named as "2007 China's Most Social Responsible Entrepreneur"

- China Shineway received another "High-Tech Industry Model Project" from the National Development and Reform Commission of PRC

- Shineway was ranked as one of the top pharmaceutical enterprises in Hebei Province consecutively for the year of 2006 & 2007

November

- Forbes Asia named China Shineway as one of Asia's Best 200 Under a Billion

December

- Wu Fu Xin Nao Qing Soft Capsules, Huo Xiang Zheng Qi Soft Capsules and Qing Kai Ling Soft Capsules are included in the honor list of 2007 with superb customer satisfaction by the Hebei Province

Chairman's Statement

Chairman of the Board
Li Zhenjiang

Dear shareholders,

On behalf of the Board of Directors of China Shineway Pharmaceutical Group Limited (the "Company" or "China Shineway") together with its subsidiaries (the "Group"), I am pleased to present the annual report of the Group for the year ended 31 December 2007.

During 2007, business growth of pharmaceutical industry resumed. Leveraged on products with superb quality and strong brand equity, the Group recorded impressive operating results. Turnover and net profit attributable to equity holders of the Group surged by approximately 20.4% and 47.3% respectively as compared to 2006. Our outstanding performance continues to be widely recognized. The Group was selected by the world-renowned Forbes Magazine as one of Asia's Best 200 Companies under a Billion for 2007.

The Group continued to develop top quality products and enhance our brand equity during the year. A number of products were able to achieve remarkable growth in sales. Among them, Shu Xie Ning injection, one of our emerging products, recorded an increase of sales by nearly two times over last year. With turnover approaching RMB100 million, the product is becoming one of our flagship products. At the same time, the Group continues to expedite investments in advanced technologies to strengthen our core competence. The construction of our new modern Chinese injection medicine workshop, located at the Group's headquarters, was completed. The new injection workshop is integrated with advanced production equipment and state-of-the-art technologies. As the new workshop was put in use in early 2008, our annual production capacity of Chinese medicine injection products has then increased to 2 billion vials, thereby further exemplifying our position as leading manufacturer of modern Chinese medicine injections. As such, a solid foundation has been laid to meet the strong demand for modern Chinese injection medicines in the coming years.

The Group continues to strengthen our capability in product research and development. During the year, we received four invention patents, and a second designation as a State Model Project of Commercialization of Advanced Technologies was granted by the National Development and Reform Commission of China. Meanwhile, our newly established Modern Technology and Quality Centre is also put in use in pursuit for further enhancement of our core competence in advanced technologies and products of superb quality.

Looking ahead, China is determined to vastly promote Chinese medicines, and has introduced a new regulatory framework for registration of Chinese medicines which will encourage innovation of modern Chinese medicines. In addition, the newly amended GMP certification standards which, together with the revised policy of medicine registration, will greatly raise the industry's entry barrier and help regulating the industry. All of these new measures will further accelerate innovation, optimize competitive environment and foster consolidation of the industry. China is expediting its investments in building basic health care facilities and expanding medical insurance coverage. Further with introduction of new rural cooperative medical insurance scheme and urban non-worker insurance policy, and increase in personal income, we should see a robust growth of medicine market and an unprecedented business opportunities for pharmaceutical companies.

Chairman's Statement

While strong growth of pharmaceutical industry is expected, China Shineway is well prepared to capture this excellent business opportunities. With strong management team, large production capacity, the Group will continue to forster market development, enhance research and development capability and increase investments in sales support and promotion and basic management to achieve excellent business growth and return for the coming years.

Appreciation

On behalf of the Board, I would like to express our gratitude for the support of our business partners, customers and shareholders, and the hard work and contribution of our employees in the past year. With our solid business foundation as well as our effort in continuous innovation, China Shineway will continue to deliver good results.

Li Zhenjiang
Chairman of the Board

Hong Kong, 26 March 2008

BUSINESS REVIEW

The sales volume of the Group's injection, soft capsule and granule products continued to expand as a result of our superb quality products, strong brand equity and effective marketing strategies. For the year ended 31 December 2007, the Group recorded a turnover growth of approximately 20.4% over 2006, amounting to approximately RMB1,012,885,000.

A breakdown of the sales by product format for the year 2007 is set out as follows:

	Sales	Growth rate	Sales mix
Injections	RMB591,663,000	26.9%	58.4%
Soft Capsules	RMB264,102,000	6.4%	26.1%
Granules	RMB137,375,000	22.7%	13.6%
Other product formats	RMB19,745,000	31.5%	1.9%

For the year ended 31 December 2007, the Group posted an increase of approximately 17.1% of operating profit to approximately RMB399,030,000 as compared to last year. Net profit attributable to the equity holders of the Group as at 31 December 2007 amounted to approximately RMB490,641,000, representing an increase of approximately 47.3% over the year of 2006. The growth in net profit was mainly attributable to the increase of turnover, gross margin and investment income during the year.

Injection Products

During the year 2007, the Group sold approximately RMB591,663,000 of injection products, an increase of approximately 26.9% over last year. Amongst these injection products, Qing Kai Ling injection, Shu Xie Ning injection, and Shen Mai injection recorded growth rates of approximately 19.8%, 176.7% and 4.1% in sales respectively. Market demand for Chinese medicine injection products continue to increase. Injection products accounted for approximately 58.4% of the Group's total turnover for 2007 as compared to approximately 52.4% of total turnover for last year. The Group believes that it is presently the largest Chinese medicine injection manufacturer in the PRC in terms of sales volume and production capacity. A number of the Group's injection products are labelled with the State protected Chinese medicine type and the status of "Good Quality/ Good Price". The new measure, "Basic technical requirement for TCM and natural medicine injection", greatly raised the standards of safety and quality control requirements of Chinese Medicine injection products. As a leading Chinese medicine injection manufacturer, the Group will be benefited from this new measure. The Group will continue to implement strategies to strengthen the development of distribution network and points of sales to increase market coverage. It is expected that Chinese medicine injection products will continue to be the product format with immense growth potential.

The Group completed a new injection workshop during the year. Our total production capacity has increased from 1.2 billion vials to two billion vials per year. As such, the Group is fully prepared for the massive demand of Chinese Medicine injection in the coming years.

Soft Capsule Products

The Group recorded sales of soft capsule products of approximately RMB264,102,000, representing an increase of approximately 6.4% over last year. Sales of Wu Fu Xin Nao Qing soft capsule and Qing Kai Ling soft capsule had increased approximately 5.4% and 78.2% respectively as compared to last year. Only Huo Xiang Zheng Qi soft capsule had declined approximately 8.1% from last year. Soft Capsule products accounted for approximately 26.1% of the Group's turnover in 2007 as compared to 29.5% in last year. The Group believes that it is currently the largest Chinese medicine soft capsule manufacturer in the PRC in terms of sales volume and production capacity. In the coming year, the Group intends to increase on advertising and promoting effort for soft capsule products to further enhance their business growth.

Granule Products

For 2007, sales of granules increased by approximately 22.7% as compared to last year, amounting to approximately RMB137,375,000. Granules produced by the Group have been popular among the public. The growth can be attributable to the Group's strategies to unify the granule brand name and market positioning. Granule products accounted for approximately 13.6% of the Group's turnover in 2007 as compared to approximately 13.3% in 2006.

Key Products

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

Sales of Qing Kai Ling injection increased by approximately 19.8% as compared to last year amounted to approximately RMB251,010,000 for the year. It accounted for approximately 24.8% of the Group's turnover. Qing Kai Ling injection is listed in the national catalogues of medical insurance and occupational injury insurance, and is designated by the State Administration of Traditional Chinese Medicine as an indispensable Chinese medicine for the emergency wards of Chinese hospitals. It is also recommended by the Ministry of Health of the PRC for treating human transmitted avian flu. The product has broad clinical applications. Qing Kai Ling injection is a famous anti-viral medicine. Qing Kai Ling injection produced by the Group was named as "Good Quality/Good Price" and "State High-Tech Products" by the state authorities. As the government is expanding health care systems and coverage in rural and urban areas, market demand for Qing Kai Ling injection is expected to increase significantly. In terms of sales volume, the Group believed that it is the largest manufacturer of Qing Kai Ling injection in the PRC. The Group will further strengthen marketing and promotion efforts at points of sales and rationalize distribution channels and to ensure the product's continuous growth.

Management Discussion and Analysis

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

Sales of Shen Mai injection was approximately RMB187,387,000 for 2007, representing an increase of approximately 4.1% from last year. The product accounted for approximately 18.5% of the Group's turnover. Shen Mai injection is a "State Protected Chinese Medicine" and is included in the national catalogues of medical insurance and occupational injury insurance. It is also recommended by the Ministry of Health of the PRC for treating human transmitted avian flu. The Group believes that it is the largest manufacturer and supplier of Shen Mai injection in China in terms of sales volume and enjoys competitive pricing advantage. The Group's Shen Mai injection is widely used in clinical applications and is very popular among medical institutions and practitioners. As the government is expanding health care systems and coverage in rural and urban areas, market demand for Shen Mai injection is expected to increase. Leveraging on strong and established brand name, and effective implementation of marketing strategy, the Group will strive to further expand market share and penetration to ensure the continuous growth in sales of Shen Mai injection.

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

As compared to last year, the sales of Wu Fu Xin Nao Qing soft capsule increased by approximately 5.4% to RMB150,178,000 accounting for approximately 14.8% of the Group's turnover for the year. Wu Fu Xin Nao Qing soft capsule is one of the lowest in cost of average daily dosage among similar cardiovascular medicines and the product has been very popular. Leveraging on its strong brand name "Wu Fu", the Group will continue to strengthen its investment and support at points of sales, and increase sales promotion to strengthen the product's growth momentum.

Emerging Products

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

Leveraged on our advanced technology in the production of high quality Chinese Medicine injections and established brand name, the Group successfully expanded the market of this product. During 2007, sales of Shu Xie Ning injection reached RMB92,142,000, representing an increase of approximately 176.7% as compared to last year. According to an independent survey, Shu Xie Ning injection, is a major clinical Chinese medicine for treating cardio-cerebrovascular disease. It is also a "State Protected Chinese Medicines" and very popular in clinical use. Shu Xie Ning injection, produced by the Group, is named as a "Good Quality/Good Price" product by state authorities and therefore enjoys certain advantages in the product sales. By riding on our advantage in production technology and economies of scale in Chinese medicine injections, this product is becoming a core product of the Group and is expected to achieve substantial growth in the coming years.

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

For 2007, sales of Huo Xiang Zheng Qi soft capsule declined by approximately 8.1% as compared to last year, with a revenue of approximately RMB50,527,000. The product accounted for approximately 5.0% of the Group's turnover for the year. The product is a "State Protected Chinese Medicine" and is listed in the national catalogues of medical insurance and occupational injury insurance. It is recommended by the Ministry of Health of the PRC for treating human transmitted avian flu. Huo Xiang Zheng Qi soft capsule is a very popular non-prescription product and enjoys a great market potential due to its effective efficacy and the high absorption rate of soft capsule. The Group will strengthen its marketing efforts and advertisement to expand market coverage. Growth for this product is expected to be resumed.

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

As compared to last year, sales of Huang Qi injection decreased by approximately 3.1% to approximately RMB29,410,000, accounting for approximately 2.9% of the Group's turnover for 2007. The product is listed in the national catalogues of medical insurance and occupational injury insurance. With the rising trend of viral myocarditis in recent years, Huang Qi injection, with a proven efficacy on such disease, has solid foundation for future market development. The lower production and sales for this year was a result of realignment of production capacity to Shu Xie Ning Injection. The Group has already increased production capacity with the new injection workshop to cope with potential market demand of the product and ensure its growth trend in the coming year.

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

Sales of Qing Kai Ling soft capsule for 2007 amounted to approximately RMB24,002,000, representing an increase of approximately 78.2% as compared to the last year. The product accounted for approximately 2.4% of the Group's turnover for the year. Qing Kai Ling soft capsule is one of the "State Protected Chinese Medicines". It is both a prescription and non-prescription medicine. It is included in the national catalogues of medical insurance and occupational injury insurance and recommended by the Ministry of Health of the PRC for treating human transmitted avian flu. With a strong brand name, effective implementation of channel strategy, points of sales pulling strategy and the brand synergy of the Qing Kai Ling injection, the Group will strengthen its promotional advertisement and marketing efforts expects that growth rate of this product can increase considerably again.

CAPITAL EXPENDITURES

During the year, the Group completed the construction of a new injection workshop to cope with the increasing demand of injection products. The total costs are approximately RMB110,000,000. The new workshop increases our average annual production output of injections from 1.2 billion vials to approximately 2.0 billion vials.

Several other projects aiming to enhance core competence and competitive edge of the Group are progressing. To enhance our research and development capability, the Group is currently establishing a new research and development center in Lang Fang, Beijing for total investment of approximately RMB33,800,000. Moreover, purchasing additional production equipment, establishment of stage 2 ERP system and construction of headquarter building are underway. Total costs for these projects are estimated to be approximately RMB180,000,000.

RESEARCH AND DEVELOPMENT

Currently, there are 29 product research projects which are either undergoing pharmaceutical and clinical trial or have completed clinical trial. Among these projects are 9 products used for treatment of various cardiovascular diseases, 3 products for treatment of digestive system illnesses and 4 products for anti-viral treatment. All of these research projects are progressed as planned.

PATENT APPLICATIONS

The Group has continuously stepped up its effort on pursuing intellectual property rights. During 2007, four inventions including "a medicine compound and its preparation method for preventing and controlling damage caused by cerebral ischemia", "an application of total triterpenes of centella asiaticain", "a modernized Chinese medicine for treatment of prostatic hyperlasis" and "a new medicine and its production know-how for treatment of chronic nephritis" developed by the Group was awarded invention patent certificates by the Intellectual Property Office of the PRC. These new patent certificates have strengthened the protection of the Group's new products and the related technologies under research to improve the Group's core competitive advantage in the long run. At present, the Group has obtained 7 patents for its inventions, and 9 invention patent applications are pending for approval.

STATE PROTECTED CHINESE MEDICINES

During 2007, the Group had twelve medicines listed as State Protected Chinese Medicines including Shen Mai injection, Shu Xie Ning injection, Guan Xin Ning injection, Huo Xian Zheng Qi soft capsule, Qing Kai Ling soft capsule, Xiao'er Qing Fei Hua Tan granules and Li Yan Jie Du granules.

CHANGES IN REGULATIONS OF THE INDUSTRY

In February 2007, Chinese regulatory authorities announced reduction of price caps on 278 Chinese medicines. Only 9 medicines of the Group were on the list, including Qing Kai Ling injection, Shu Xie Ning injection, Deng Zhan Hua Su injection and Guan Xin Ning injection. Because these four injection products are labeled as "Good Quality/Good Price", the decreases of price caps for them are less than the other brands without such label. The Group believes that decreases of price caps stated in the insurance catalog will not have material impact on its earnings because average retail prices of most of our products remain lower than the current price caps.

Chinese government has expressed its intention to support modernization of Chinese medicines. To further regulate and guide the work of research and quality control of Chinese medicines injection, the State Food and Drug Administration promulgated the "Basic Technological Requirements on Chinese Medicines and Natural Medicine Injections" (中藥、天然藥物注射劑基本技術要求). The new measure serves to regulate Chinese medicine injections in a more standardized and scientific manner and provides more specific and detailed guidelines on safety and effectiveness. The new requirements will also increase entry barrier of the production of modern Chinese medicine injection and accelerate consolidation of the industry.

During the year, the State Food and Drug Administration also promulgated the newly amended "Inspection and Assessment Standards of GMP Certification for Medicines" (藥品GMP認證檢查評定標準). The amended GMP standards further tighten requirements on pharmaceutical manufacturers in a more rigid manner and enhances the quality control of production. In addition, the new "Administrative Measures for Drug Registration" (藥品註冊管理辦法) took effect on 1 October 2007. It will encourage enterprises to commercialize R&D results, reduce the scope of meaning of new medicines, extend the time of drugs approval, and raise the barrier of entry to the industry. As such, pharmaceutical manufacturers with strong competitive strength will stand out, and enjoy greater potential to grow.

PROSPECT

Driven by medical reform and increase in market demand, pharmaceutical industry will continue to grow in 2008. While details of medical reform have not yet been announced, direction of the reform is generally expected to focus on accelerating the establishment of a basic medical and health care system for urban and rural residents and to safeguard their livelihood. The ultimate goal is to provide a basic medical coverage for every one in China in the coming years.

With a growing but also ageing population, the consumption in medical care will undoubtedly keep increasing in China. The forthcoming medical reform will bring new strength into the medicine industry. Medical and health care coverage will continue to be broadened. Market and demand of medicines will surge as more health care facilities are being built. Medical reform will certainly provide tremendous potential for the pharmaceutical market. And for modern Chinese medicine industry, this presents a great prospect.

Chinese medicine is the national treasure of China. It is also an integral part of the Chinese medical system. Chinese medicine industry enjoys its advantage imbedded in the Chinese culture. With reference to a number of initiatives set out in the "11th Five-Year Plan of High-tech Industrial Development" issued in the year, the Framework of Development for Modernization of Chinese Medicine (中藥現代化發展綱要) (2002-2010) and Framework of Innovations for Chinese Medicine (中醫藥創新發展規劃綱要) (2006-2020), as well as the Basic Technological Requirements on Chinese Medicines and Natural Medicine Injections(中藥、天然藥物注射劑基本技術要求) and Supplementary Regulations for Chinese Medicine Registration (中藥註冊管理補充規定) issued and took effect recently, Chinese government is determined on the development of Chinese medicines, leading to fast growing momentum in the industry.

Supporting measures provided by amended or new regulations on modern Chinese medicine industry provide a great driving force for modern Chinese medicine products. In the years ahead, the Group will continue to safeguard the health of Chinese people by providing modern Chinese medicines of good efficacy and superb quality with affordable price.

GROWTH STRATEGIES

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

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

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

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

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

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

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

FINANCIAL ANALYSIS

Turnover

In 2007, the Group continued to focus its business on modern Chinese medicine products of high quality. A number of our products were able to achieve remarkable growth in sales. Accordingly, the Group recorded a growth of 20.4% in total turnover as compared with last year. Turnover of injection amounted to approximately RMB591,663,000, representing an increase of around 26.9% as compared with 2006 and accounting for approximately 58.4% of the Group's turnover. Turnover of soft capsule products amounted to approximately RMB264,102,000, representing an increase of around 6.4% over last year and accounting for approximately 26.1% of the Group's turnover. Turnover of granule products amounted to approximately RMB137,375,000, representing an increase of around 22.7% over last year and accounting for approximately 13.6% of the Group's turnover. Turnover of the Group's products of other formats amounted approximately RMB19,745,000, accounting for approximately 1.9% of the Group's turnover.

Turnover of the 3 key products of the Group are as follows: Shen Mai injection increased by approximately 4.1% from 2006 to approximately RMB187,387,000; Qing Kai Ling injection increased by approximately 19.8% from 2006 to approximately RMB251,010,000, and Wu Fu Xin Nao Qing soft capsule increased by about 5.4% from 2006 to approximately RMB150,178,000.

During the year, turnover of medicines for treating cardiovascular diseases, anti-viral medicines, gastroenterological medicines and medicines for treating other illness accounted for approximately 51.4% (2006: 51.8%), 30.8% (2006: 29.5%), 5.0% (2006: 6.5%) and 12.8% (2006: 12.2%) of the Group's total turnover, respectively.

Turnover of prescription and non-prescription medicines of the Group of 2007 were approximately RMB832,484,000 and RMB180,401,000, accounting for approximately 82.2% and 17.8% of the total turnover, respectively.

As at 31 December 2007, the Group had 34 products that were included in the medical insurance catalogue.

Cost of Sales

Cost of sales of the Group in 2007 was approximately RMB274,847,000, accounting for approximately 27.1% of the total turnover. Direct materials, direct labour and other production costs accounted for approximately 73.2%, 5.9% and 20.9% of the total cost of sales.

Gross Profit Margin

During 2007, the overall gross profit margin of the Group increased from 70.4% to approximately 72.9% as compared to last year. The average gross profit margins of injection products, soft capsule products and granule products were approximately 77.4%, 75.7% and 50.2%, respectively. The improvement in gross profit margin is mainly attributable to the economies of scale, effective internal control, and advanced production technology to achieve high extraction rate and production yield rate. The high gross profit margin for the emerging products promoted by the Group also led to the increase in the gross profit margin of the Group during the year.

Investment Income

During 2007, the Group allocated a portion of funds generated from PRC operation to invest in the "A" share market of PRC to increase return of the Group's cash balance. The dividends and net gain from such held-for-trading investments were RMB2,213,000 and RMB166,688,000 respectively. As at 31 December 2007 of the balance sheet date, the Group disposed all held-for-trading investments.

Distribution Costs

During the 2007, the overall distribution costs of the Group increased by approximately 40.4% compared to last year, representing approximately 25.5% (2006: 21.8%) of the Group's turnover. This was primarily attributable to the increase of distributor promotion expenses by approximately 56.1%. Distributor promotion expenses which accounted for approximately 15.0% (2006: 11.4%) of turnover, mainly included the promotion cost subsidies to distributors. The Group had been strengthening its effort in promotion of products by exploring potential markets in eastern China and southern China and had been actively participating in exhibitions, seminars and trainings, resulting in increased promotion cost subsidies to distributors and related promotion costs.

Administrative Expenses

The administrative expenses of the Group increased by approximately 19.5% in 2007 when compared with last year, representing approximately 8.0% (2006: 8.0%) of the Group's turnover. The increase of the administrative expenses was mainly due to the increase of research and development expenses by around 34.1% from last year. The research and development expenses for 2007 accounted for approximately 0.5% (2006: 0.4%) of the Group's turnover.

Administrative expenses also comprised of non-productive depreciation expenses of fixed assets which accounted for approximately 0.6% (2006: 0.3%) of the Group's total turnover.

Income Tax Rate

On 16 March 2007, the PRC promulgated the Law of the People's Republic of China on Enterprise Income Tax (the "New Law") by Order No. 63 of the President of the PRC. On 6 December 2007, the State Council of the PRC issued Implementation Regulations of the New Law. The New Law and Implementation Regulations will change the tax rate from 33% to 25% for certain subsidiaries from 1 January 2008. The deferred tax balance has been adjusted to reflect the tax rates that are expected to apply to the respective periods when the asset is realized or the liability is settled.

Pursuant to the relevant law and regulations in the PRC, Shineway Pharmaceutical Co., Ltd. ("Shineway Pharmaceutical") and Hebei Shineway Pharmaceutical Co., Ltd. ("Hebei Shineway") are entitled to a 50% relief from PRC Enterprise Income Tax ("PRC EIT") for current year and the following year. The first profitable period of Shineway Pharmaceutical and Hebei Shineway commenced from 1 January 2004, and their PRC EITs for those years ended 31 December 2005 were all exempted.

Pursuant to National Tax Document 1998 No. 26 (國發1998 26號), the PRC Enterprise Income Tax rate applicable to Shineway Sales was 15% of its assessable profit.

Pursuant to the 藏財稅字(94) 117號, Xizang Shineway Pharmaceutical Co., Ltd. ("Xizang Shineway") was exempted from the PRC EIT for the period from 21 May 2007 to 20 May 2008. Pursuant to 西藏拉薩經濟技術開發區優惠政策, the PRC EIT rate applicable to Xizang Shineway is 10% on its assessable profit.

Pursuant to 國發1988 26號, the PRC EIT rate applicable to Shineway Pharmaceutical (Hainan) Co., Limited ("Hainan Shineway") is 15% on its assessable profit.

As the year of 2007 was the fourth profitable year for Shineway Pharmaceutical and Hebei Shineway, the overall income tax payable increased from 13.9% to approximately 14.8% compared to last year. The overall effective income tax rate of the Group from 2006 to 2008 is estimated to be approximately 15%.

Dividends

Details of dividends and dividend policy are set out in the director's report on page 24 of this annual report.

Capital Structure

By the year ended 31 December 2007, there was no change in the capital structure and issued share capital of the Group.

Establishment of Subsidiaries

In 2007, the Group has established two wholly-owned subsidiaries namely Xizang Shineway Pharmaceutical Co., Ltd and Shineway Pharmaceutical (Hainan) Co., Ltd, with registered share capital of US$1,250,000 and US$3,900,000 respectively. These two wholly-owned subsidiaries were incorporated in PRC, with principal activity of trading Chinese pharmaceutical products.

Liquidity and Financial Resources

As at 31 December 2007, bank deposits of the Group approximately amounted to RMB1,678,442,000 (2006: RMB1,582,014,000), which mainly comprised of approximately RMB1,142,934,000, HK$283,953,000 and US$38,643,000 (equivalent to approximately RMB264,076,000 and 280,313,000 respectively). Except for trade and other payables, the Group did not have any other liabilities.

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

Trade and Bills Receivables

As at 31 December 2007, bills receivables has increased by approximately 286.8% as compared with 31 December 2006. Turnover days of trade and bills receivables were 2.2 days and 55.5 days (2006: 1.4 days and 42.9 days respectively).

Inventories

Inventories balance as at 31 December 2007 increased by approximately 105.1% as compared with 31 December 2006 due to an expected increase in demand of sales in the beginning of 2008. As at 31 December 2007, raw materials, work in progress and finished goods accounted for approximately 40.6%, 27.4% and 32.0% (2006: 35.9%, 29.9% and 34.2%) of inventories respectively.

Finished goods inventories turnover days of 2007 were 25.3 days (2006: 19.0 days).

Management Discussion and Analysis

Property, Plant and Equipment

As at 31 December 2007, property, plant and equipment increased by approximately 24.1% as compared with last year.

Goodwill

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

Trade Payables

During the period under review, turnover days of trade payables was 109.8 days (2006: 138.0 days).

Loans and Bank Borrowings

The Group did not have any loans or bank borrowings as at 31 December 2007 (2006: Nil). Accordingly, the gearing ratio based on interest bearing debt for the year is Nil (2006: Nil).

Contingent Liabilities

The Group did not have any contingent liabilities as at 31 December 2007 (2006: Nil).

Exposure to Fluctuations in Exchange Rates

Several subsidiaries of the Company have foreign currency bank balances, which expose the Group to foreign currency risk. Approximately 30% of the Group's bank balances are denominated in currencies other than the functional currency of the group entity. Substantially all of the business transactions and liabilities of the Group are denominated in Renminbi and Hong Kong dollars. The Group adopts a conservative financial policy and majority of its bank deposits are in Renminbi and Hong Kong dollars. As at 31 December 2007, the Group did not have any bank liabilities, foreign exchange contracts, interest or currency swaps or other financial derivatives for hedging purpose.

Connected Transaction

On 1 March 2007, a wholly-owned subsidiary of the Group entered into a share transfer agreement with Shineway Medical Science & Technology (Lang Fang) Co., Ltd ("Shineway Lang Fang") for the acquisition of the research and development center and the relevant land use rights for an aggregate consideration of RMB23,960,000. Shineway Lang Fang is a 70% subsidiary of Shineway Medical Science & Technology Co., Ltd ("Shineway Medical"), which is controlled by a director of the Company.

Employees

As at 31 December 2007, the Group has 2,307 (2006: 2,155) employees. Remuneration was determined and reviewed based on fair principles with reference to market conditions and individual performance. The Group also provided other benefits to its employees, including medical insurance and retirement benefits. The Group's employees in Hong Kong were also enrolled in the mandatory provident fund scheme.

Directors and Senior Management

DIRECTORS

Executive Directors

LI Zhenjiang (李振江), aged 52, is an executive Director and one of the founders of the Group. Mr. Li obtained an EMBA degree from the Yangtze Commercial Institute. Mr. Li joined the predecessor of the Group in 1974 and has been the Chairman and President of the Group and its predecessor since 1984 with responsibility for business development and strategy. He has more than 20 years' experience in the operation and management of modern Chinese medicine enterprises. Mr. Li takes charge of the overall management of the Group and is also specifically responsible for the Group's research and development activities. Mr. Li is a Representative to the 10th and 11th National People's Congress. He was named as an Outstanding Entrepreneur in the PRC Pharmaceutical Industry in 1994, and as an Academician of Asian Knowledge Management Association in 2005 and has received a National Wu Yi Labour Award and special subsidies of the State Council. Mr. Li is the vice-chairman of the PRC Chinese Medicine Association. Mr. Li is also directors of several members of the Group.

WANG Zhihua (王志華) (alias 王志花), aged 52, is an executive Director and one of the founders of the Group. Ms. Wang graduated from Hebei Province Finance School in 1978 where she majored in industrial accountancy. Ms. Wang is primarily responsible for the Group's financial strategy and management. Ms. Wang joined the predecessor of the Group in 1982, where she focused on financial matters. She was the Deputy General Manager (finance and management) of Shineway Medical immediately prior to the corporate reorganisation in preparation of the listing of the Company in 2004. Ms. Wang has more than 20 years' experience in the industry with the Group.

XIN Yunxia (信蘊霞), aged 44, is an executive Director and one of the founders of the Group. Ms. Xin graduated from the Yangtze Commercial Institute with an EMBA degree. Ms. Xin is primarily responsible for the Group's human resources management and operation. Ms. Xin joined the predecessor of the Group in 1981, focused on administration. She was the Deputy General Manager (human resources management) of Shineway Medical immediately prior to the corporate reorganisation in preparation of the listing of the Company in 2004. Ms. Xin has more than 20 years experience in business management in the industry with the Group.

LI Huimin (李惠民), aged 40, an executive Director, graduated from Hebei Party School in 1997 where he majored in economic administration. He is primarily responsible for the marketing and sales of the Group's products and, since joining the Group in 1992, focused on sales and marketing. Immediately prior to the corporate reorganisation in preparation of the listing of the Company in 2004, Mr. Li was the sales and marketing manager of Shineway Medical. He has developed a deep understanding of sales management in the PRC Chinese medicine industry with more than 12 years' experience.

Directors and Senior Management

HUNG Randy King Kuen (孔敬權), aged 42, is an executive Director. He is a fellow certified public accountant and holds a bachelor's degree of science in accounting and a certificate of programming and data processing from the University of Southern California, a certificate of China Accounting, Finance, Taxation and Law from the Chinese University of Hong Kong and a Hong Kong Securities Institute Specialist Certificate in corporate finance. Mr. Hung joined the Group in June 2005 and is primarily responsible for corporate development and investor relation of the Group. Mr. Hung is a fellow of the Hong Kong Institute of Certified Public Accountants, a member of the American Institute of Certified Public Accountants, a member of the Hong Kong Securities Institutes and council member of the Hong Kong Institute of Directors. Mr. Hung is currently an independent non-executive director of two Hong Kong listed companies.

Independent Non-Executive Directors

REN Dequan (任德權), aged 64, an independent non-executive Director, graduated from East China Chemical Industry Institute (now known as East China Engineering University). He has previously served as the deputy general manager of China Medicinal Herbs Corporation, director of science and technology education of National Medicine Administrative Bureau, general manager of China Pharmaceuticals Corporation, assistant commissioner of National Chinese Medicine Administrative Bureau and assistant commissioner of National Drugs Surveillance Administrative Bureau. From March, 2003 to March, 2005, he was appointed as assistant commissioner of National Food and Drugs Surveillance Administrative Bureau. In 2005, he has retired and was appointed as the honorary president of the Modern Chinese Medicine International Association. In November 2006, he was appointed as non-executive director of Shenzhen Neptunus Interlong Bio-technique Company Limited (Stock Code: 8329). Mr. Ren was appointed as an independent non-executive Director of the Company on 3 July 2006.

LI Kung Man (李公民), aged 51, an independent non-executive Director, is a fellow of the Chartered Association of Certified Accountants in the United Kingdom and an associate of the Hong Kong Institute of Certified Public Accountants. He graduated from Hong Kong Polytechnic University in 1980 with a Higher Diploma in Accountancy (HKICPA/ACCA). Mr. Li Kung Man has accumulated over 20 years' experience in accounting and finance and has previously worked for CLP Holdings Ltd (Stock Code: 002) and PricewaterhouseCoopers. He is currently a director of Freeway International Holdings Limited and Dewelty Mobile Limited. He was also an independent non-executive director of Guangdong Kelon Electrical Holdings Company Limited (Stock Code: 921) up to 26 June 2006, a company listed on the Main Board of the Stock Exchange, and AKM Industrial Company Limited (Stock Code: 8298), a company listed on the Growth Enterprise Market of the Stock Exchange. Mr. Li Kung Man was appointed as an independent non-executive Director in November 2004.

CHENG Li (程麗), aged 48, an independent non-executive Director, is a partner of Commerce & Finance Law Office. She has a legal science bachelor's degree and the legal science master's degree from the law department of Japan Specially Repairs University. She also studied in Japan and Chinese Investment Trade Promotion Association. She joined Commerce & Finance Law Office in 1995 and became a partner of Commerce & Finance Law Office in 2005. She is currently a member of Beijing Lawyer Association. Ms. Cheng was appointed as an independent non-executive Director of the Company on 3 July 2006.

SENIOR MANAGEMENT

CHEN Zhong (陳鍾), aged 41, graduated from Hebei Medical University in 1990 with a bachelor's degree in pharmacy. He joined the Group in 1990. From 1990 to 1992, Mr. Chen was responsible for development of new products. After spending two years managing the tablet workshop from 1993 to 1994, he managed the production technology division until 1997 and was then appointed the Chief Engineer for production from 1997 to 1999. Since 1999, Mr. Chen has been a Deputy General Manager responsible for production. Mr. Chen is responsible for the Group's production management and technology development.

WANG Qinli (王欽禮), aged 45, graduated from Henan Chinese Medical Institute with a bachelor's degree in Chinese medicine in 1986. Prior to joining the Group, Mr. Wang spent 10 years, from 1986 to 1996, working in technology and new medicine research at a pharmaceutical manufacturer in Henan Province, the PRC, where he reached the post of Head of New Medicine Research and Head of Technology Department. Mr. Wang joined the Group in 1996 as manager of the research and development department, and then was promoted to Deputy General Manager in 2003, responsible for overseeing the Group's quality control and research and development activities.

TSE Tak Kwong (謝德光), aged 51, is the Financial Controller of the Group. Mr. Tse obtained a Certificate in Accounting from the City College of Commerce in 1976. He joined the Group in 2003, prior to which he worked for an international accounting firm from 1979 to 2000. Between 2001 and 2003, Mr. Tse worked as a consultant providing accounting services. He has more than 20 years' experience in finance and accountancy.

QUALIFIED ACCOUNTANT AND COMPANY SECRETARY

WONG Mei Shan (汪美珊), aged 33, is the qualified accountant and Company Secretary of the Group. Ms. Wong is a Certified Public Accountant of Hong Kong Institute of Certified Public Accountants. She has a bachelor degree in Accounting from the University of Science and Technology and a bachelor of Laws from the University of London. Ms. Wong joined the Group in 2006 and has extensive working experience in accounting. She has worked in a subsidiary of a listed company in Hong Kong as an accountant for 3 years. Prior to that, she had worked in two international accounting firms for 5 years and was an Assistant Manager when she left in 2002.

Directors' Report

The Board of Directors (the "Board") is pleased to present to the shareholders their annual report and the audited financial statements of the Company and its subsidiaries (hereinafter collectively referred to as the "Group") for the year ended 31 December 2007.

PRINCIPAL ACTIVITIES

The Company acts as an investment holding company. The principal activities of its subsidiaries are research, development, manufacture and trading of modern Chinese medicines.

RESULTS

The results of the Group for the year ended 31 December 2007, prepared in accordance with the international accounting standards, are set out in the consolidated income statements on page 46 of this annual report.

DIVIDENDS

On 20 March 2006, the Board approved a dividend policy to distribute interim and final dividends to all the shareholders of the Company of not less than 40% of the distributable profit of the year.

An interim dividend of RMB11 cents per share, amounting to RMB90,970,000, was paid to the shareholders on 18 September 2007.

The Board now recommends to pay a final dividend of RMB11 cents per share and a special dividend of RMB16 cents per share for the year ended 31 December 2007 to the shareholders on the register of members of the Company on 28 April 2008. The proposed final and special dividends will be voted by shareholders at the annual shareholders' meeting to be held on 28 April 2008.

Paid interim dividend and recommended final and special dividends during 2007 in aggregate, amounting to RMB38 cents, are equal to approximately 64.1% of net profit attributable to shareholders of 2007.

FINANCIAL HIGHLIGHTS

A summary of the results and assets and liabilities for the last five years, as extracted from the relevant audited financial statements, is set out on page 3 of this annual report. The summary does not form part of the audited financial statements.

PROPERTY, PLANT AND EQUIPMENT

Details of the movement in the property, plant and equipment of the Group during the year are set out in note 14 to the financial statements.

SHARE CAPITAL AND RESERVE

Details of the movement in share capital and reserve of the Company during the year are set out in the consolidated statement of changes in equity and also in note 24 and note 26 to the financial statements. At the balance sheet date, the Company's reserves available for distribution to shareholders amounted to RMB1,246,151,000 (2006: RMB1,124,815,000). The Company has not issued any shares during the year.

DEBENTURES

The Company has not issued any debentures during the year.

DIRECTORS

The directors of the Company during the year and up to the date of this report were:

Executive Directors:

Mr. Li Zhenjiang
Ms. Wang Zhihua
Ms. Xin Yunxia
Mr. Li Huimin
Mr. Hung Randy King Kuen

Independent Non-Executive Directors:

Mr. Ren Dequan
Mr. Li Kung Man
Ms. Cheng Li

The biographical details of the directors are set out on page 21 to page 22 of this annual report.

Each of Mr. Li Zhenjiang, Ms. Wang Zhihua, Ms. Xin Yunxia and Mr. Li Huimin has entered into a service contract with the Company for a term of two years commencing from 1 October 2006, and Mr. Hung Randy King Kuen has entered into a service contract with the Company for a term commencing from 7 June 2005 to 31 May 2008. Each service contract will continue thereafter until terminated by not less than three months' notice in writing served by either party on the other.

Each of the independent non-executive directors, except for Mr. Li Kung Man, has been appointed for a term of two years. Mr. Li Kung Man has not been appointed for any specific terms, however, he is subject to retirement by rotation and re-election at the Company's annual general meeting in accordance with the Company's Bye-laws. The appointment of each of the independent non-executive directors is subject to retirement by rotation in accordance with the Company's Articles of Association.

Other than disclosed above, none of the directors has entered or has proposed to enter into any service contract with the Company or any of its subsidiaries which is not expiring or determinable by the employing company within one year without payment of compensation other than statutory compensation.

The Company had received confirmation from each of the independent non-executive directors of their independence pursuant to Rule 3.13 of the Rules Governing the Listing of Securities on the Stock Exchange and considered all independent non-executive directors to be independent.

Pursuant to Article 87(1) of the Company's Articles of Association, Mr. Li Zhenjiang, Ms. Wang Zhihua, Mr. Hung Randy King Kuen and Mr. Li Kung Man will retire, being eligible for re-election, and offer themselves for re-election at the forthcoming annual general meeting.

Detail of directors' emoluments on a named basis are set out in note 10 to the financial statements on page 67 of this annual report.

DIRECTORS' INTERESTS IN CONTRACTS

Save as disclosed in note 30 to the financial statements, no contracts of significance to which the Company, any of its holding companies, fellow subsidiaries or subsidiaries was a party and in which a director of the Company had a material interest, whether directly or indirectly, subsisted at the end of the year or at any time during the year.

DIRECTORS' INTERESTS IN SHARES

As at 31 December 2007, the interests and short positions of the Directors and their respective associates in the shares, underlying shares and debentures of the Company and its associated corporations within the meaning of Part XV of the Securities and Futures Ordinance (the "SFO"), which are required to be notified to the Company and the Stock Exchange pursuant to Divisions 7 and 8 of Part XV of the SFO (including interests and short positions which they are taken or deemed to have under such provisions of the SFO) or which are required pursuant to section 352 of the SFO, to be entered in the register referred therein, or which are required, pursuant to the Model Code for Securities Transactions by Directors of Listed Issuers to be notified to the Company and the Stock Exchange were as follows: Mr. Li Zhenjiang, a Director, is deemed to be interested in 600,000,000 Shares representing approximately 72.55% of the issued share capital of the Company. These 600,000,000 Shares are held by Sinovest International Investment Limited, which is owned as to approximately 79.40% by Forway Investment Limited ("Forway"). Forway is owned as to 100% by Trustcorp Limited, a trust company, in its capacity as the trustee of The Li Family 2004 Trust. The Li Family 2004 Trust is a discretionary trust, the founder (as defined in the SFO) of which is Mr. Li Zhenjiang and the discretionary objects of which are family members of Mr. Li Zhenjiang (excluding Mr. Li Zhenjiang himself). Accordingly, Mr. Li Zhenjiang is deemed to be interested in the 600,000,000 Shares under the SFO.

Save as disclosed above, as at 31 December 2007, none of the directors of the Company or their respective associates had any interest or short position in the shares, underlying shares or debentures of the Company or any of its associated corporations.

DIRECTORS' RIGHTS TO ACQUIRE SHARES OR DEBENTURES

At no time during the year was the Company, its holding company or any of its subsidiaries a party to any arrangement to enable the directors of the Company to acquire benefits by means of the acquisition of shares in, or debentures of, the Company or any other body corporate.

SUBSTANTIAL SHAREHOLDERS

(a) Interest in the Company

As at 31 December 2007, interest of every person (not being a director or chief executive of the Company) in the shares and underlying shares in the Company as recorded in the register required to be kept by the Company under Section 336 of the SFO were as follows:

Name of shareholder	Capacity	Number of shares held	Approximate percentage of shareholding in the Company
Sinovest International Investment Limited ("Sinovest") (Notes 1 and 2)	Beneficial owner	600,000,000	72.55%
Forway Investment Limited ("Forway") (Notes 1, 2 and 3)	Interest of a controlled corporation	600,000,000	72.55%
Trustcorp Limited (Notes 1 to 4)	Trustee of discretionary trust	600,000,000	72.55%
David Henry Christopher HILL (Notes 1 and 5)	Interest of controlled corporation	600,000,000	72.55%
David William ROBERTS (Notes 1 and 6)	Interest of controlled corporation	600,000,000	72.55%
Rebecca Ann HILL (Notes 1, 5 and 7)	Interest of spouse	600,000,000	72.55%

Notes:

(1) All interests of Sinovest, Forway, Trustcorp Limited, David Henry Christopher HILL, David William ROBERTS and Rebecca Ann HILL in the share of the Company were duplicated.

(2) The 600,000,000 shares of the Company are beneficially owned by Sinovest.

(3) The issued share capital of Sinovest is owned as to approximately 79.4% by Forway. Accordingly Forway is deemed to be interested in the 600,000,000 shares of the Company under the SFO.

(4) The entire issued share capital of Forway is owned by Trustcorp Limited in its capacity as the trustee of The Li Family 2004 Trust, a discretionary trust the founder (as defined in the SFO) of which is Li Zhenjiang and the discretionary objects of which are family members of Li Zhenjiang (excluding Li Zhenjiang himself). Accordingly, Trustcorp Limited is deemed to be interested in the 600,000,000 shares of the Company under the SFO.

(5) The following is a breakdown of the interests in shares held by David Henry Christopher HILL:

			Total interest in Shares	
Name of controlled corporation	**Name of controlling shareholder**	**Percentage of control**	**Direct interest**	**Indirect interest**
Newcorp Holdings Ltd.	David Henry Christopher HILL	35	–	600,000,000
Newcorp Ltd.	Newcorp Holdings Ltd.	100	–	600,000,000
Trustcorp Limited	Newcorp Ltd.	100	–	600,000,000
Forway Investment Limited	Trustcorp Limited	100	–	600,000,000
Sinovest International Investment Limited	Forway Investment Limited	79.4	600,000,000	–

(6) The following is a breakdown of the interests in shares held by David William ROBERTS:

			Total interest in Shares	
Name of controlled corporation	**Name of controlling shareholder**	**Percentage of control**	**Direct interest**	**Indirect interest**
Newcorp Holdings Ltd.	David William Roberts	35	–	600,000,000
Newcorp Ltd.	Newcorp Holdings Ltd.	100	–	600,000,000
Trustcorp Limited	Newcorp Ltd.	100	–	600,000,000
Forway Investment Limited	Trustcorp Limited	100	–	600,000,000
Sinovest International Investment Limited	Forway Investment Limited	79.4	600,000,000	–

(7) This interest is in fact the same block of 600,000,000 shares of the Company as disclosed by David Henry Christopher HILL.

(b) Interest in other members of the Group

As at 31 December 2007, so far as the directors or the chief executives of the Company are aware, no person will be directly or indirectly interested in 5% or more of the nominal value of any class of shares carrying rights to vote in general meetings of any other member of the Group.

As at 31 December 2007, the Company had not been notified by any persons who had interests or short positions in the shares or underlying shares of the Company which would fall to be disclosed to the Company under Divisions 2 and 3 of Part XV of the SFO.

SHARE OPTION SCHEME

The existing share option scheme (the "Scheme"), which was adopted by the Company pursuant to a written resolution of the sole shareholder of the Company passed on 10 November 2004 is for the primary purpose of providing a flexible means of giving incentives to, rewarding, remunerating, compensating and/or providing benefits to the following participants, and for such other purposes as the Board may approve from time to time:

(i) any executive or non-executive director including any independent non-executive director or any employee (whether full-time or part-time) of any member of the Group;

(ii) any discretionary object of a discretionary trust established by any substantial shareholder of the Company or any employee, executive or non-executive director of any member of the Group;

(iii) any consultant, professional and other advisers to any member of the Group;

(iv) any chief executive or substantial shareholder of any member of the Group;

(v) any Associate of any director, chief executive or substantial shareholder of any member of the Group; and

(vi) any employee (whether full-time or part-time) of substantial shareholder of any member of the Group to take up Options.

The total number of shares in respect of which options may be granted under the Scheme is 82,700,000 shares, which is equivalent to 10% of the total number of shares of the Company in issue on the date of commencement of dealings in the shares of the Company on the Stock Exchange.

The maximum number of shares of the Company issued and to be issued upon exercise of the options granted to each participant (including both exercised and unexercised options) under the Scheme and any other share option scheme (if any) adopted by the Company in any 12-month period must not exceed 1% of the shares of the Company in issue unless otherwise approved by the Company's shareholders. Where any grant of options to a substantial shareholder, an independent non-executive director, or any of their respective associates (including a discretionary trust whose discretionary objects include a substantial shareholder or an independent non-executive director or a company beneficially owned by any substantial shareholder or independent non-executive director of the Company) would result in the shares of the Company issued and to be issued upon exercise of all options already granted and to be granted to such person in any 12-month period up to and including the date of the grant:

(i) representing in aggregate over 0.1% of the shares of the Company in issue; and

(ii) having an aggregate value, based on the closing price of the shares of the Company as stated in the daily quotations sheets issued by the Stock Exchange on the date of grant in excess of HK$5 million, such grant of option shall be subject to prior approval of the shareholders of the Company who are not connected persons of the Company as defined in the Rules Governing the Listing of Securities on the Stock Exchange (the "Listing Rules").

An option must be exercised within 10 years from the date of grant or such shorter period as the Board may notify to the grantee.

Option granted must be taken up within 14 days from the date of offer, upon payment of HK$1 per option. Options may be exercise at any time from the date of grant of the share option to the 10th anniversary of the date of grant. The exercise price is determined by the directors of the Company, and will not be less than the higher of (i) the closing price of the Company's shares on the date of grant, (ii) the average closing price of the shares for the five business days immediately preceding the date of grant; and (iii) the nominal value of the Company's share.

The Scheme has a life of 10 years and will expire on 9 November 2014 unless otherwise terminated in accordance with the terms of the Scheme.

However, no option was granted, exercised, cancelled or lapsed during the year and as at the date of this report since adoption.

PURCHASE, SALE OR REDEMPTION OF SHARES

During the year ended 31 December 2007, the Company or its subsidiaries did not purchase, sell or redeem any shares of the Company.

PRE-EMPTIVE RIGHTS

There are no provisions for pre-emptive rights under the Company's Articles of Association although there are no restrictions against such rights under the laws in the Cayman Islands.

MAJOR CUSTOMERS AND SUPPLIERS

The aggregate sales attributable to the largest customer and five largest customers of the Group were 5.1% and 17.3% respectively of the Group's turnover for the year.

The aggregate purchases attributable to the largest supplier and five largest suppliers of the Group were 4.5% and 19.9% respectively of the Group's purchases for the year.

None of the directors, their associates, or any shareholder (which to the knowledge of the directors owns more than 5% of the Company share capital) has any interests in the five largest customers or suppliers of the Group.

CONNECTED TRANSACTIONS

Pursuant to the supply agreement dated 20 November 2004 between Shineway Sales, a subsidiary of the Company, and 河北神威大藥房連鎖有限公司(Hebei Shineway Chain Drugstores Co., Ltd.) ("Shineway Drugstores"), a connected person of the Company by virtue of being ultimately controlled by Mr. Li Zhenjiang, an executive director of the Company, Shineway Sales had agreed to supply Shineway Drugstores with pharmaceutical products for a term of two years and nine months commencing on 1 April 2004 until 31 December 2006 in accordance with the terms of the sale and purchase contracts entered into between the parties from time to time during the term of the agreement. The continuing connected transaction contemplated under this supply agreement is subject to reporting, announcement and independent shareholders' approval requirements, but waiver from strict compliance therewith (except the reporting requirement) has been obtained from the Stock Exchange. For the year ended 31 December 2006, the total sales by Shineway Sales to Shineway Drugstores amounted to RMB277,000 (equivalent to approximately HK$274,257), which did not exceed the annual cap of RMB11,000,000 (equivalent to approximately HK$10,891,000) prescribed for the year ended 31 December 2006 as disclosed in the Prospectus.

On 29 December 2006, Shineway Sales and Shineway Drugstores entered into a new supply agreement (the "New Supply Agreement"). According to the New Supply Agreement, the total amount of the annual sales by Shineway Sales to Shineway Drugstores will not exceed RMB1,000,000 for each of 3 years ending until 31 December 2009. The continuing connected transaction under the New Supply Agreement falls within the de minimis exemption under Rule 14A.33(3) of the Listing Rules and is therefore exempt from the reporting, announcement and independent shareholders' approval requirements under the Listing Rules. For the year ended 31 December 2007, there was no sales by Shineway Sales to Shineway Drugstores.

On 1 March 2007, Hebei Shineway, a wholly-owned subsidiary of the Company entered into a transfer agreement with Shineway Lang Fang for the acquisition of the research and development center and the relevant land use rights for an aggregate consideration of RMB23,960,000.

Mr. Li Zhenjiang, Director of the Company, is the controlling shareholder of Shineway Medical, which holds 70% equity interest in Shineway Lang Fang. Accordingly, Shineway Lang Fang is a connected person of the Company within the meaning of the Listing Rules. As a result, the acquisition constitutes a connected transaction for the Company. As the consideration is less than 2.5% for each of the percentage ratios (except the profits ratio) under Rule 14.07 of the Listing Rules, the acquisition is exempt from independent shareholders' approval under Rule 14A.32 of the Listing Rules and is only subject to the reporting and announcement requirements under Rules 14A.45 to 14A.47 of the Listing Rules.

The independent non-executive directors of the Company have reviewed the connected transactions disclosed above and have considered the procedures performed by the auditors of the Company in reviewing them and confirmed that:

(a) the transactions have been entered into by the relevant member of the Group in the ordinary and usual course of business of the Group;

(b) the transactions have been entered into on an arm's length basis and on normal commercial terms (to the extend that there are comparable transactions) or, if there are not sufficient comparable transactions to judge whether they are on normal commercial terms, or terms not less favourable to the Group than terms available to or from (as the case may be) independent third parties; and

(c) the transactions have been entered into in accordance with the relevant agreement governing them on terms that are fair and reasonable and in the interests of the shareholders of the Company as a whole.

MANAGEMENT CONTRACTS

Except for the connected transactions as stated in this directors' report, no contracts concerning the management and administration of the whole or any substantial part of the business of the Company were entered into or existed during the year.

EMOLUMENT POLICY

The emolument policy of the employees of the Group is set up by the Remuneration Committee on the basis of their merit, qualification and competence.

The emolument of the directors of the Company are decided by the Remuneration Committee, having regard to the Company's operating results, individual performance and comparable market statistics.

The directors' fees, basic salaries, housing allowances, other allowances and benefits in kind are disclosed in note 10 to the financial statements.

The contributions to pension schemes for directors and past directors for the financial year are disclosed in note 10 to the financial statements.

Pursuant to the directors' service contracts with the Company, all executive directors' annual salary, except one, will increase as from 1 January 2008 at an incremental rate of 5% per annum. All executive director, except one, may be entitled to a discretionary bonus to be determined by the Board (or its duly appointed remuneration committee) at its absolute discretion having regard to the performance of the Group, provided that the aggregate amount of the bonus payable to those directors in respect of any financial year shall not exceed 5% of the audited consolidated net profit after taxation but before extraordinary items of the Company for the relevant financial year.

There were no compensation paid during the financial year or receivable by directors or past directors for the loss of office as a director of any member of the Group or of any other office in connection with the management of the affairs of any member of the Group distinguishing between contractual and other payments.

PENSION SCHEMES

The pension schemes of the Company and its subsidiaries are primarily in form of contributions to the Hong Kong mandatory provident fund and China statutory public welfare fund.

SUFFICIENCY OF PUBLIC FLOAT

The Company has maintained a sufficient public float throughout the year of 2007.

CHARITABLE DONATIONS

During the year, neither the Company nor its subsidiaries made charitable and other donations.

AUDITORS

During the year, Messrs. Deloitte Touche Tohmatsu were appointed as auditors of the Company. A resolution will be submitted to the annual general meeting to re-appoint Messrs. Deloitte Touche Tohmatsu as auditors of the Company.

On behalf of the Board

LI ZHENJIANG
CHAIRMAN OF THE BOARD

Hong Kong, 26 March 2008

Dear Shareholders,

China Shineway Pharmaceutical Group Limited (the "Company") and its subsidiaries (collective referred to as the "Group") are firmly committed to statutory and regulatory corporate governance standards and adhere to the principles of corporate governance emphasising transparency, independence, accountability, responsibility and fairness.

The Board of Directors (the "Board" or the "Directors") believes that good corporate governance practices are an essential element in guiding the growth and management of the business of the Group. Therefore the Board reviews its corporate governance practices from time to time to ensure that they protect the shareholders' interest, comply with legal and professional standards and reflect the latest local and international circumstances and development. The Board will continue to commit itself to achieving a high quality of corporate governance.

CODE ON CORPORATE GOVERNANCE PRACTICES

The Company has, throughout the year ended 31 December 2007 and up to the date of publication of this annual report, applied and complied with the principles in the Code on Corporate Governance Practices (the "Code") set out in Appendix 14 of the Listing Rules, except for the deviations as stated in paragraphs headed "Chairman and Chief Executive Officer" and "Independent Non-Executive Directors" below.

DIRECTORS' SECURITIES TRANSACTIONS

The Company has adopted the full set of Model Code set out in Appendix 10 of the Listing Rules as the code of conduct for securities transactions by directors (the "Model Code"). The prohibitions on securities dealing and disclosure requirements in the Model Code apply to specified individuals including the Group's senior management and also persons who are privy to price sensitive information of the Group. The interests in the Company's securities held by the Directors as at 31 December 2007 as set out on page 27 and the extent of applications of the Model Code are disclosed in this Corporate Governance Report. Based on specific inquiries made by the company secretary of the Company, all directors confirmed that they had complied with the Model Code regarding directors' securities transactions during the year and up to the date of publication of the Annual Report.

THE BOARD OF DIRECTORS

The Board of Directors represents shareholders in overseeing the Group's business. The Directors recognise their responsibilities to enhance shareholders' value and to conduct themselves in accordance with their duty of care and loyalty.

Throughout the financial year ended 31 December 2007, the Board had eight directors consisting of five Executive Directors and three Independent Non-executive Directors. Pursuant to the requirements of the Listing Rules, the Company has received written confirmation from each Independent Non-Executive Director of his/her independence. The Group considered them to be independent. The names of the directors and their respective biographies are set out on pages 21 to 22 of this annual report. The information is also published on the Company's websites.

Corporate Governance Report

The Board oversees the Group's strategic development, and determines the objectives, strategies and policies of the Group. The Board also monitors and controls operating and financial performance in pursuit of the Group's strategic objectives. All Board members have access to appropriate business documents and information about the Group on a timely basis. All directors and board committees have access to external legal counsel and other professionals for independent advice at the Group's expense if they require it.

Two board committees, namely, the audit committee and the remuneration committee, have been established to oversee particular aspects of the Group's affairs. The Board has delegated the day-to-day management and operations of the Group's businesses to the management of the Company and its subsidiaries respectively. Major corporate matters that are specifically delegated by the Board to the management include the preparation of financial statements for board approval before publishing, execution of business strategies and initiatives adopted by the Board, implementation of adequate systems of internal controls and risk management procedures, and compliance with relevant statutory requirements, rules and regulations.

The Board had met four times this year to review the financial performance of the Group, major issues (whether or not required by the Listing Rules) and also on other occasions when board decisions were required. The views of Independent Non-Executive Directors were actively solicited by the Group if they were unable to attend meetings of the Board.

The major issues which were brought before the Board for their decisions during the year include:

1. formulation of operational strategies and review of its financial performance and results and the internal control system;

2. policies relating to key business and financial objectives of the Group;

3. proposals related to potential acquisitions, investments, or any significant capital expenditures; and

4. the declaration of any interim dividend and recommendation to shareholders on final dividend.

The names of the directors and individual attendance of each director at each board meeting is as follows:

	Attendance
Executive Directors	
Mr. Li Zhenjiang *(Chairman of the Board)*	4/4
Ms. Wang Zhihua	4/4
Ms. Xin Yunxia	4/4
Mr. Li Huimin	4/4
Mr. Hung Randy King Kuen	4/4
Independent Non-executive Directors	
Mr. Ren Dequan	4/4
Mr. Li Kung Man	4/4
Ms. Cheng Li	4/4

The Directors acknowledged that they are responsible for the preparation of the accounts which give a true and fair view of the affairs of the Group. The auditors are responsible to form an independent opinion, based on their audits, on the Group's financial statements and express their opinions.

The Board has the overall responsibility to ensure that the Company maintains sound and effective internal controls to safeguard the shareholders' investments and the Company's assets. The internal audit department has been conducting regular review of the system's effectiveness and reports to the Directors and the audit committee on its material findings.

CHAIRMAN AND CHIEF EXECUTIVE OFFICER

The Code provision A.2.1 stipulated that the roles of chairman of the board (the "Chairman") and chief executive officer should be separate and should not be performed by the same individual. The division of responsibilities between the Chairman and chief executive officer should be clearly established and set out in writing. The Company does not use the title "Chief Executive Officer". The duty of Chief Executive Officer has been assumed by the President of the Company.

Mr. Li Zhenjiang has been both the Chairman and President of the Company, his responsibilities are clearly set out in writing and approved by the Board. Given the Group's current stage of development, the Board considers that vesting the roles of Chairman and President in the same person facilitates the execution of the Group's business strategies and maximizes effectiveness of its operations. The Board shall nevertheless review the structure from time to time and shall consider the appropriate adjustment should new circumstance arise.

INDEPENDENT NON-EXECUTIVE DIRECTORS

Each of the independent non-executive directors, except for Mr. Li Kung Man, has entered into an appointment letter with the Company for a term of two years commencing from 3 July 2006 or till retirement by rotation in accordance with the Company's Articles of Association, if earlier.

Mr. Li Kung Man has not been appointed for any specific terms, however, he is subject to retirement by rotation and re-election at the Company's annual general meeting in accordance with the Company's Bye-laws.

REMUNERATION OF DIRECTORS

The Company established a remuneration committee on 10 November 2004 with written terms of reference as disclosed on the Company's websites. The primary duties of the remuneration committee include the following:

I. To make recommendation to the Board on (a) the Company's policy and structure for all remuneration of directors and senior management, and (b) the Company's establishment of a formal and transparent procedure for developing policy on such remuneration;

2. To determine the specific remuneration packages of all Executive Directors, and senior management, including benefits in kind, pension right, compensation payment (including any compensation for loss or termination of office or appointment);

3. To make recommendation to the Board on the remuneration of Non-executive Directors;

4. To have due consideration of all relevant factors such as salaries paid by comparable companies, time commitment and responsibilities of the Directors, employment conditions elsewhere in the Group and desirability of performance-based remuneration;

5. To review and approve performance-based remuneration by reference to corporate goals and objectives resolved by the Board from time to time;

6. To review and approve the compensation payable to Executive Directors and senior management in connection with any loss or termination of their office or appointment to ensure that such compensation is determined in accordance with relevant contractual terms and that such compensation is otherwise fair and not excessive for the Company;

7. To review and approve the compensation arrangements relating to dismissal or removal of directors for misconduct to ensure that such arrangements are determined in accordance with relevant contractual terms and that any compensation payment is otherwise reasonable and appropriate;

8. To ensure that no director or any of his associates is involved in deciding his own remuneration.

During the year under review, the members of remuneration committee comprised independent non-executive Directors Ms. Cheng Li and Mr. Li Kung Man, and an executive Director Ms. Xin Yunxia. Ms. Cheng Li is the chairman of the remuneration committee. The remuneration committee met on two occasions during the year to consider and approve the service contracts of executive Directors, review the long term incentive scheme of the Group, and assess the performance of executive directors.

Individual attendance of each remuneration committee member is as follows:

	Attendance
Ms. Cheng Li *(Chairman)*	2/2
Mr. Li Kung Man	2/2
Ms. Xin Yunxia	2/2

The emolument policy of the employees of the Group was set up by the Remuneration Committee on the basis of their merit, qualification and competence.

The emolument of the directors of the Company are determined by the Remuneration Committee, having regard to the Group's operating results, individual performance and comparable market statistics.

Further details on the emolument policy and basis of determining the emolument payable to the Directors are disclosed on page 33 of this annual report.

The Group's stock option scheme as described on page 30 of this annual report is adopted as the Group's long term incentive scheme.

NOMINATION OF DIRECTORS

The Directors are aware of their collective and individual responsibilities to its shareholders for the well-being and success of the Company. During the year under review, the Executive Directors are charged with the responsibility to consider and to assess candidates for directorships on the Board based on their characters, qualifications and experience appropriate for the businesses of the Group. The recommendations of the Executive Directors are then put forward for consideration and adoption by the board as a whole, including Independent Non-Executive Directors.

All Directors are appointed for a fixed term except for Mr. Li Kung Man, who has not been appointed on a fixed term. The Articles of Association of the Company required that one-third of the Directors (including Executive and Non-Executive Directors) shall retire each year. The Directors to retire each year shall be those appointed by the Board during the year and those who have been longest in office since their election or re-election. A retiring director is eligible for re-election.

INTERNAL CONTROL

The Board is responsible for ensuring that sound and effective internal control systems are maintained within the Group. The Company and its subsidiaries have adopted a set of internal control procedures and policies to safeguard the assets, to ensure proper maintenance of accounting records and reliability of financial reporting, and to ensure compliance with relevant legislation and regulations. The internal control systems are designed to ensure that the financial and operational functions, compliance control, material control, asset management and risk management functions are in place and functioning effectively.

The Board and the audit committee have delegated the Group's internal audit department to conduct periodic review of the effectiveness of the internal control systems of the Company and its subsidiaries, covering all material controls, including financial, operational and compliance controls as well as risk management functions.

Based on the assessments made by the Group's internal audit department, the Board considered that the internal control systems of the Company and its subsidiaries are effective and the audit committee have found no material deficiencies on the internal control based on the assessments made by the Group's internal audit department.

AUDITORS' REMUNERATION

Annually since 2004, Deloitte Touche Tohmatsu has been appointed as the Group's external auditors by shareholders. During the year, the fees charged to the accounts of the Company and its subsidiaries for Deloitte Touche Tohmatsu's statutory audit services amounted to HK$1,480,000 (2006: HK$1,350,000), and in addition to a total of HK$368,000 (2006: HK$339,000) for other services, including the review of interim financial statements.

AUDIT COMMITTEE

The audit committee members comprise Mr. Li Kung Man, Ms. Cheng Li and Mr. Ren Dequan. All of the members of the audit committee are Independent Non-Executive Directors. Mr. Li Kung Man, who has appropriate professional qualifications or accounting or related financial management expertise, is the chairman of the audit committee. No member of this committee is a member of the former or external auditors of the Company. The committee members possess diversified industry experience.

The audit committee's primary responsibilities include overseeing the relationship with the Company's external auditors, review of financial information of the Group, and oversight of the Group's financial reporting system, internal control procedures and risk management. The Company has adopted a term of reference of the audit committee on which complies with the provisions of the Code. The terms of reference of the audit committee is available on the Company's website.

Individual attendance of each audit committee member during the year is as follows:

	Attendance
Mr. Li Kung Man *(Chairman)*	2/2
Mr. Ren Dequan	2/2
Ms. Cheng Li	2/2

The audit committee met on two occasions during the year and the report on the work performed by the audit committee can be found on page 43 of this annual report.

COMMUNICATION WITH SHAREHOLDERS

The Group attaches great priority to communicate with shareholders and investors. Since our listing on the Main Board of the Exchange in December 2004, the Group has regularly met with investors to increase corporate transparency. During the year, the Group met and/or held telephone conferences with a number of investors and participated in institutional investor conferences. We issued two voluntary announcements. We held a number of site visits for investors. Since June 2005, we have distributed "Shineway Newsflash" to investors on a monthly basis.

To foster effective communications, the Company provides extensive information in its annual report, interim report, press releases and also disseminates information relating to the Group and its business electronically through its websites.

Since October 2005, to enable the shareholders to better evaluate the operations and performance of the Group, the Group has been announcing quarterly financial Information on turnover in due course after the relevant period ended.

Corporate Governance Report

The Company regards the Annual General Meeting ("AGM") as an important event as it provides an important opportunity for direct communication between the Board and shareholders. Directors and senior management will make an effort to attend the AGM. The Chairman of the Board, as well as the Chairmans of audit committee and remuneration committee and external auditors will be available during the AGM to address shareholders' queries. All shareholders are given at least 21 days' notice of the AGM and they are encouraged to attend the AGM and other shareholders' meetings. Questioning by the shareholders at such meetings are encouraged and welcomed.

CODE OF CONDUCT

Employees of the Group have maintained high level of ethical standards. The Group published an employee handbook, setting out standards of professional and ethical conduct for all employees of the Group. Trainings on the contents of the Employee Handbook have been held regularly. The employees at all levels are expected to act in an honest, diligent and responsible manner.

Audit Committee Report

Dear Shareholders,

The committee formally met two times during the year and other informal meetings were conducted as and when necessary. These meetings were held together with senior management and external auditors as and when necessary, to consider the external auditors' proposed audit fees, their independence and scope of the audit; review the internal control and risk management systems; review the interim and annual financial statements, particularly judgmental areas, accounting principles and practice adopted by the Group; review the external auditors' management letter and management's response; and review the Group's adherence to the Code on Corporate Governance Practices as set out at Appendix 14 of the Listing Rules.

The audit committee recommended the Board to reappoint Deloitte Touche Tohmatsu as external auditors for the fiscal year 2008 and recommended to approve the interim and annual reports.

MEMBERS OF AUDIT COMMITTEE

Mr. Li Kung Man *(Chairman)*
Mr. Ren Dequan
Ms. Cheng Li

26 March 2008

Independent Auditor's Report

Deloitte.
德勤

TO THE MEMBERS OF CHINA SHINEWAY PHARMACEUTICAL GROUP LIMITED

中國神威藥業集團有限公司
(incorporated in the Cayman Islands with limited liability)

We have audited the consolidated financial statements of China Shineway Pharmaceutical Group Limited (the "Company") and its subsidiaries (collectively referred to as the "Group") set out on pages 46 to 86, which comprise the consolidated balance sheet as at 31 December 2007, and the consolidated income statement, the consolidated statement of changes in equity and the consolidated cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes.

Directors' responsibility for the consolidated financial statements

The directors of the Company are responsible for the preparation and the true and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards. This responsibility includes designing, implementing and maintaining internal control relevant to the preparation and the true and fair presentation of the consolidated financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditor's responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit and to report our opinion solely to you, as a body, in accordance with our agreed terms of engagement, and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report. We conducted our audit in accordance with Hong Kong Standards on Auditing issued by the Hong Kong Institute of Certified Public Accountants. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance as to whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and true and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the directors, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements give a true and fair view of the state of affairs of the Group as at 31 December 2007 and of the Group's profit and cash flows for the year then ended in accordance with International Financial Reporting Standards and have been properly prepared in accordance with the disclosure requirements of the Hong Kong Companies Ordinance.

Deloitte Touche Tohmatsu
Certified Public Accountants
Hong Kong
26 March 2008

Consolidated Income Statement

For the year ended 31 December 2007

	Notes	2007 RMB'000	2006 RMB'000
Turnover	7	**1,012,885**	841,475
Cost of sales		**(274,847)**	(249,175)
Gross profit		**738,038**	592,300
Investment income	8	**207,241**	44,779
Other income		**26,644**	1,523
Distribution costs		**(258,079)**	(183,848)
Net exchange loss		**(56,974)**	–
Other administrative expenses		**(80,929)**	(67,720)
Profit before taxation	9	**575,941**	387,034
Income tax	11	**(85,300)**	(54,057)
Profit for the year		**490,641**	332,977
Earnings per share – basic	12	**RMB0.59**	RMB0.40
Dividends recognised as distribution during the year:	13		
Final dividend		**82,700**	82,700
Special dividend		**16,540**	16,540
Interim dividend		**90,970**	82,700
		190,210	181,940
Dividends proposed:			
Final dividend		**90,970**	82,700
Special dividend		**132,320**	16,540
		223,290	99,240

Consolidated Balance Sheet

At 31 December 2007

	Notes	2007 RMB'000	2006 RMB'000
Non-current assets			
Property, plant and equipment	14	**278,547**	224,368
Land use rights	15	**19,894**	5,618
Goodwill	16	**58,479**	58,479
Deferred tax assets	17	**7,329**	9,198
		364,249	297,663
Current assets			
Inventories	18	**78,352**	38,197
Bills receivables	19	**244,820**	63,301
Trade receivables	19	**8,865**	3,346
Prepayment, deposits and other receivables		**34,009**	21,340
Pledged bank deposits	20	**–**	1,882
Bank balances and cash	19	**1,678,442**	1,582,014
		2,044,488	1,710,080
Current liabilities			
Trade payables	21	**89,172**	76,146
Other payables and accrued expenses		**198,095**	142,388
Amounts due to related companies	22	**10,063**	587
Government grants received	23	**6,380**	5,800
Tax liabilities		**35,752**	13,569
		339,462	238,490
Net current assets		**1,705,026**	1,471,590
Total assets less current liabilities		**2,069,275**	1,769,253
Capital and reserves			
Share capital	24	**87,662**	87,662
Reserves	26	**1,981,613**	1,681,591
Total equity		**2,069,275**	1,769,253

The financial statements on pages 46 to 86 were approved and authorised for issue by the Board of Directors on 26 March 2008 and are signed on its behalf by:

LI ZHENJIANG	**WANG ZHIHUA**
Director	*Director*

Consolidated Statement of Changes in Equity

For the year ended 31 December 2007

	Share capital RMB'000 (note 24)	Share premium RMB'000	Merger reserve RMB'000 (note 26)	Exchange reserve RMB'000	Statutory surplus reserve fund RMB'000 (note 26)	Statutory public welfare fund RMB'000 (note 26)	Discretionary surplus reserve fund RMB'000 (note 26)	Accumulated profits RMB'000	Total RMB'000
At 1 January 2006	87,662	982,408	83,758	(20,689)	74,408	37,206	121,000	264,495	1,630,248
Exchange differences arising on translation of foreign operations	–	–	–	(12,032)	–	–	–	–	(12,032)
Profit for the year	–	–	–	–	–	–	–	332,977	332,977
Net income recognised for the year	–	–	–	(12,032)	–	–	–	332,977	320,945
Transfers	–	–	–	–	66,884	(37,206)	–	(29,678)	–
Dividends paid	–	–	–	–	–	–	–	(181,940)	(181,940)
At 1 January 2007	87,662	982,408	83,758	(32,721)	141,292	–	121,000	385,854	1,769,253
Exchange differences arising on translation of foreign operations	–	–	–	(409)	–	–	–	–	(409)
Profit for the year	–	–	–	–	–	–	–	490,641	490,641
Net income recognised for the year	–	–	–	(409)	–	–	–	490,641	490,232
Transfers	–	–	–	–	68,711	–	11,000	(79,711)	–
Dividends paid	–	–	–	–	–	–	–	(190,210)	(190,210)
At 31 December 2007	87,662	982,408	83,758	(33,130)	210,003	–	132,000	606,574	2,069,275

Consolidated Cash Flow Statement

For the year ended 31 December 2007

	2007 RMB'000	2006 RMB'000
Operating activities		
Profit before taxation	**575,941**	387,034
Adjustments for:		
Depreciation of property, plant and equipment	**32,084**	29,733
Gain on disposal of property, plant and equipment	**–**	(28)
Interest income	**(38,340)**	(44,779)
Operating lease rentals in respect of land use rights	**675**	328
Unrealised exchange loss	**61,824**	–
Operating cash flows before movements in working capital	**632,184**	372,288
Increase in inventories	**(40,155)**	(2,746)
(Increase) decrease in bills receivables	**(181,519)**	71,047
(Increase) decrease in trade and other receivables, prepayment and deposits	**(16,493)**	5,371
Decrease in amount due from a related company	**–**	155
Increase in trade and other payables and accrued expenses	**68,733**	11,837
Increase in amounts due to related companies	**468**	587
Cash generated from operations	**463,218**	458,539
PRC Enterprise Income Tax paid	**(61,248)**	(41,130)
Net cash from operating activities	**401,970**	417,409
Investing activities		
Decrease (increase) in pledged bank deposits	**1,882**	(1,882)
Government grants received	**580**	400
Interest received	**36,645**	35,334
Purchase of property, plant and equipment	**(86,325)**	(23,219)
Purchase of land use rights	**(6,290)**	–
Proceeds from disposal of property, plant and equipment	**–**	314
Net cash (used in) from investing activities	**(53,508)**	10,947
Financing activity		
Dividends paid	**(190,210)**	(181,940)
Cash used in financing activity	**(190,210)**	(181,940)
Net increase in cash and cash equivalents	**158,252**	246,416
Cash and cash equivalents at beginning of the year	**1,582,014**	1,347,605
Effect of exchange rate changes	**(61,824)**	(12,007)
Cash and cash equivalents at end of the year, representing bank balances and cash	**1,678,442**	1,582,014

Notes to the Financial Statements

For the year ended 31 December 2007

1. GENERAL

The Company was incorporated and registered as an exempted company with limited liability in the Cayman Islands under the Companies Law (2001 Second Revision) Chapter 22 of the Cayman Islands on 14 August 2002 and its shares have been listed on the Mainboard of The Stock Exchange of Hong Kong Limited (the "Stock Exchange"). Its parent is Sinovest International Investment Limited, a company incorporated in the British Virgin Islands ("BVI") with limited liability and owned as to approximately 79.4% by Forway Investment Limited, which is considered the ultimate holding company of the Company. The address of the registered office and principal place of business of the Company are disclosed in the "Corporate Information" section to the annual report.

The consolidated financial statements are presented in Renminbi ("RMB"), which is the functional currency of the Company.

The Company acts as an investment holding company. The principal activities of its principal subsidiaries are set out in the note 31 to the consolidated financial statements.

2. APPLICATION OF NEW AND REVISED INTERNATIONAL FINANCIAL REPORTING STANDARDS ("IFRSs")

In the current year, the Group has applied, for the first time, the following new standard, amendment and interpretations ("new IFRSs") issued by the International Accounting Standards Board ("IASB") and the International Financial Reporting Interpretations Committee ("IFRIC") of the IASB which are effective for the Group's financial year beginning 1 January 2007.

IAS 1 (Amendment)	Capital disclosures
IFRS 7	Financial instruments: Disclosures
IFRIC 7	Applying the restatement approach under IAS 29 Financial reporting in hyperinflationary economies
IFRIC 8	Scope of IFRS 2
IFRIC 9	Reassessment of embedded derivatives
IFRIC 10	Interim financial reporting and impairment

The application of the new IFRSs had no material effect on how the results and the financial position for the current or prior periods have been prepared and presented. Accordingly, no prior period adjustment has been required. The Group has applied the disclosure requirements under IAS 1 (Amendment) and IFRS 7 retrospectively. Certain information based on the requirements of IAS 32 has been removed and the relevant comparative information based on the requirements of IAS 1 (Amendment) and IFRS 7 has been presented for the first time in the current year.

2. APPLICATION OF NEW AND REVISED INTERNATIONAL FINANCIAL REPORTING STANDARDS ("IFRSs") *(continued)*

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

IAS 1 (Revised)	Presentation of financial statements[1]
IAS 23 (Revised)	Borrowing costs[1]
IAS 27 (Revised)	Consolidated and separate financial statements[5]
IAS 32 & 1 (Amendments)	Puttable instruments and obligations arising on liquidation[1]
IFRS 2 (Amendments)	Vesting conditions and cancellations[1]
IFRS 3 (Revised)	Business combinations[5]
IFRS 8	Operating segments[1]
IFRIC 11	IFRS 2: Group and treasury share transactions[2]
IFRIC 12	Service concession arrangements[3]
IFRIC 13	Customer loyalty programmes[4]
IFRIC 14	IAS 19 – The limit on a defined benefit asset, minimum funding requirements and their interaction[3]

1 Effective for annual periods beginning on or after 1 January 2009.
2 Effective for annual periods beginning on or after 1 March 2007.
3 Effective for annual periods beginning on or after 1 January 2008.
4 Effective for annual periods beginning on or after 1 July 2008.
5 Effective for annual periods beginning on or after 1 July 2009.

3. SIGNIFICANT ACCOUNTING POLICIES

The consolidated financial statements have been prepared in accordance with IFRSs issued by the IASB and the IFRIC. In addition, the consolidated financial statements include applicable disclosures required by the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited and by the Hong Kong Companies Ordinance.

The consolidated financial statements have been prepared on the historical cost basis except for certain financial instruments, which are measured at fair values, as explained in the principal accounting policies set out below.

Basis of consolidation

The consolidated financial statements incorporate the financial statements of the Company and entities controlled by the Company (its subsidiaries). Control is achieved where the Company has the power to govern the financial and operating policies of an entity so as to obtain benefit from its activities.

3. SIGNIFICANT ACCOUNTING POLICIES *(continued)*

Basis of consolidation *(continued)*

The results of subsidiaries acquired or disposed of during the year are included in the consolidated income statement from the effective date of acquisition or up to the effective date of disposal, as appropriate.

Where necessary, adjustments are made to the financial statements of subsidiaries to bring their accounting policies into line with those used by other members of the Group.

All intra-group transactions, balances, income and expenses are eliminated on consolidation.

Business combinations

The acquisition of businesses is accounted for using the purchase method. The cost of the acquisition is measured at the aggregate of the fair values, at the date of exchange, of assets given, liabilities incurred or assumed, and equity instruments issued by the Group in exchange for control of the acquiree, plus any costs directly attributable to the business combination. The acquiree's identifiable assets, liabilities and contingent liabilities that meet the conditions for recognition under IFRS 3 Business Combinations are recognised at their fair values at the acquisition date.

Goodwill arising on acquisition is recognised as an asset and initially measured at cost, being the excess of the cost of the business combination over the Group's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities recognised. If, after reassessment, the Group's interest in the net fair value of the acquiree's identifiable assets, liabilities and contingent liabilities exceeds the cost of the business combination, the excess is recognised immediately in consolidated income statement.

Revenue recognition

Revenue is measured at the fair value of the consideration received or receivable and represents amounts receivable for goods sold in the normal course of business, net of discounts and sales related taxes.

Revenue from sales of goods are recognised when goods are delivered and title has passed.

Interest income from a financial asset is accrued on a time basis, by reference to the principal outstanding and at the effective interest rate applicable, which is the rate that exactly discounts the estimated future cash receipts through the expected life of the financial asset to that asset's net carrying amount.

3. SIGNIFICANT ACCOUNTING POLICIES *(continued)*

Property, plant and equipment

Property, plant and equipment, other than construction in progress, are stated at cost less subsequent accumulated depreciation and accumulated impairment losses.

Depreciation is provided to write off the cost of items of property, plant and equipment other than construction in progress over their estimated useful lives and after taking into account of their estimated residual value, using the straight line method.

Construction in progress includes property, plant and equipment in the course of construction for production or for its own use purposes. Construction in progress is stated at cost less any recognised impairment loss. Construction in progress is classified to the appropriate category of property, plant and equipment when completed and ready for intended use. Depreciation of these assets, on the same basis as other property assets, commences when the assets are ready for their intended use.

An item of property, plant and equipment is recognised upon disposal or when no future economic benefits are expected to arise from the continued use of the asset. Any gain or loss arising on derecognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the item) is included in the consolidated income statement in the year in which the item is derecognised.

Land use rights

Payments for obtaining land use rights are considered as operating lease payment and charged to consolidated income statement over the period of the right using the straight line method.

Goodwill

Goodwill arising from an acquisition of a business represents the excess of the cost of acquisition over the Group's interest in the fair value of the identifiable assets, liabilities and contingent liabilities of the relevant business recognised at the date of acquisition. Such goodwill is carried at cost less any accumulated impairment losses.

Capitalised goodwill arising from an acquisition of a business is presented separately in the consolidated balance sheet.

3. SIGNIFICANT ACCOUNTING POLICIES *(continued)*

Goodwill *(continued)*

For the purpose of impairment testing, goodwill arising from an acquisition is allocated to each of the relevant cash-generating units expected to benefit from the synergies of the combination. Cash-generating units to which goodwill has been allocated are tested for impairment annually, or more frequently when there is an indication that the unit may be impaired. If the recoverable amount of the cash-generating unit is less than the carrying amount of the unit, the impairment loss is allocated first to reduce the carrying amount of any goodwill allocated to the unit and then to the other assets of the unit pro-rata on the basis of the carrying amount of each asset in the unit. An impairment loss recognised for goodwill is not reversed in a subsequent period.

On subsequent disposal of the relevant cash-generating unit, the attributable amount of goodwill is included in the determination of the profit or loss on disposal.

Research and development expenditure

Expenditure on research activities is recognised as an expense in the period in which it is incurred.

An internally-generated intangible asset arising from development (or from the development phase of an internal project) is recognised if, and only if, all of the following have been demonstrated:

- the technical feasibility of completing the intangible asset so that it will be available for use or sale;
- the intention to complete the intangible asset and use or sell it;
- the ability to use or sell the intangible asset;
- how the intangible asset will generate probable future economic benefits;
- the availability of adequate technical, financial and other resources to complete the development and to use or sell the intangible asset; and
- the ability to measure reliably the expenditure attributable to the intangible asset during its development.

The amount initially recognised for internally-generated intangible assets is the sum of the expenditure incurred from the date when the intangible asset first meets the recognition criteria listed above. Where no internally-generated intangible asset can be recognised, development expenditure is charged to profit or loss in the period in which it is incurred.

3. SIGNIFICANT ACCOUNTING POLICIES *(continued)*

Inventories

Inventories are stated at the lower of cost and net realisable value. Cost, which comprises all costs of purchase and, where applicable, costs of conversion and other costs that have been incurred in bringing the inventories to their present location and condition, is calculated using the first-in first-out method. Net realisable value represents the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sale.

Impairment of assets excluding goodwill

At each balance sheet date, the Group reviews the carrying amounts of its assets to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss (if any). Where it is not possible to estimate the recoverable amount of an individual asset, the Group estimates the recoverable amount of the cash-generating unit to which the asset belongs.

Recoverable amount is the higher of fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset for which the estimates of future cash flows have not been adjusted.

If the recoverable amount of an asset is estimated to be less than its carrying amount, the carrying amount of the asset is reduced to its recoverable amount. Impairment losses are recognised as an expense immediately.

Where an impairment loss subsequently reverses, the carrying amount of the asset is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset (cash-generating unit) in prior years. A reversal of an impairment loss is recognised as income immediately.

Financial instruments

Financial assets

Investments are recognised and derecognised on trade date where the purchase or sale of an investment is under a contract whose terms require delivery of the investment within the timeframe established by the market concerned, and are initially measured at fair value, plus transaction costs, except for those financial assets classified as at fair value through profit or loss, which are initially measured at fair value.

3. SIGNIFICANT ACCOUNTING POLICIES *(continued)*

Financial instruments *(continued)*

Financial assets *(continued)*

Financial assets are classified into the following specified categories: trade receivables, bills receivables, other receivables and bank balances. The classification depends on the nature and purpose of the financial assets and is determined at the time of initial recognition.

Effective interest method

The effective interest method is a method of calculating the amortised cost of a financial asset and of allocating interest income over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash receipts (including all fees on points paid or received that form an integral part of the effective interest rate, transaction costs and other premiums or discounts) through the expected life of the financial asset, or, where appropriate, a shorter period.

Income is recognised on an effective interest basis for debt instruments.

Held-for-trading investments

A financial asset is classified as held for trading if:

- it has been acquired principally for the purpose of selling in the near future; or
- it is a part of an identified portfolio of financial instruments that the Group manages together and has a recent actual pattern of short-term profit-taking; or
- it is a derivative that is not designated and effective as a hedging instrument.

Held for trading investments are stated at fair value, with any resultant gain or loss recognised in profit or loss. The net gain or loss recognised in profit or loss incorporates any dividend or interest earned on the financial asset.

Loans and receivables

Bills receivables, trade and other receivables and bank balances that have fixed or determinable payments that are not quoted in an active market are classified as loans and receivables. Loans and receivables are measured at amortised cost using the effective interest method, less any impairment. Interest income is recognised by applying the effective interest rate, except for short-term receivables when the recognition of interest would be immaterial.

3. SIGNIFICANT ACCOUNTING POLICIES *(continued)*

Financial instruments *(continued)*

Impairment of financial assets

Financial assets, other than held-for-trading investments, are assessed for indicators of impairment at each balance sheet date. Financial assets are impaired where there is objective evidence that, as a result of one or more events that occurred after the initial recognition of the financial asset, the estimated future cash flows of the investment have been impacted.

For certain categories of financial asset, such as trade receivables, assets that are assessed not to be impaired individually are subsequently assessed for impairment on a collective basis. Objective evidence of impairment for a portfolio of receivables could include the Group's past experience of collecting payments, an increase in the number of delayed payments in the portfolio past the average credit period normally ranging from six months to one year, as well as observable changes in national or local economic conditions that correlate with default on receivables.

For financial assets carried at amortised cost, the amount of the impairment is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the financial asset's original effective interest rate.

The carrying amount of the financial asset is reduced by the impairment loss directly for all financial assets with the exception of trade receivables, where the carrying amount is reduced through the use of an allowance account. When a trade receivable is considered uncollectible, it is written off against the allowance account. Subsequent recoveries of amounts previously written off are credited against the allowance account. Changes in the carrying amount of the allowance account are recognised in profit or loss.

In a subsequent period, if the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is reversed through profit or loss to the extent that the carrying amount of the investment at the date the impairment is reversed does not exceed what the amortised cost would have been had the impairment not been recognised.

Financial liabilities and equity

Financial liabilities and equity instruments issued by a group entity are classified according to the substance of the contractual arrangements entered into and the definitions of a financial liability and an equity instrument.

An equity instrument is any contract that evidences a residual interest in the assets of the group after deducting all of its liabilities. Equity instruments issued by the Company are recorded at the proceeds received, net of direct issue costs.

3. SIGNIFICANT ACCOUNTING POLICIES *(continued)*

Financial instruments *(continued)*

Effective interest method

The effective interest method is a method of calculating the amortised cost of a financial liability and of allocating interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments through the expected life of the financial liability, or, where appropriate, a shorter period.

Interest expense is recognised on an effective interest basis.

Financial liabilities

Financial liabilities including trade and other payables and amounts due to related companies are subsequently measured at amortised cost, using the effective interest method.

Derecognition

Financial assets are derecognised when the rights to receive cash flows from the assets expire or, the financial assets are transferred and the Group has transferred substantially all the risks and rewards of ownership of the financial assets. On derecognition of a financial asset, the difference between the asset's carrying amount and the sum of the consideration received and receivable and the cumulative gain or loss that had been recognised directly in equity is recognised in profit or loss.

Financial liabilities are derecognised when the obligation specified in the relevant contract is discharged, cancelled or expires. The difference between the carrying amount of the financial liability derecognised and the consideration paid and payable is recognised in profit or loss.

Government grants

Government grants are recognised as income over the periods necessary to match them with the related costs. Grants related to expense items are recognised in the same period as those expenses are charged in the consolidated income statement and are deducted in reporting the related expenses.

Retirement benefit costs

Payments to defined contribution retirement benefit plans are charged as an expense when employees have rendered service entitling them to the contributions.

3. SIGNIFICANT ACCOUNTING POLICIES *(continued)*

Taxation

Income tax expense represents the sum of the tax currently payable and deferred tax.

The tax currently payable is based on taxable profit for the year. Taxable profit differs from profit as reported in the consolidated income statement because it excludes items of income and expense that are taxable or deductible in other years, and it further excludes income statement items that are never taxable and deductible. The Group's liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the balance sheet date.

Deferred tax is recognised on differences between the carrying amounts of assets and liabilities in the consolidated financial statements and the corresponding tax bases used in the computation of taxable profit, and is accounted for using the balance sheet liability method. Deferred tax liabilities are generally recognised for all taxable temporary differences, and deferred tax assets are recognised to the extent that it is probable that taxable profits will be available against which deductible temporary differences can be utilised. Such assets and liabilities are not recognised if the temporary difference arises from goodwill or from the initial recognition (other than in a business combination) of other assets and liabilities in a transaction that affects neither the taxable profit nor the accounting profit.

The carrying amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered.

Deferred tax is calculated at the tax rates that are expected to apply in the period when the liability is settled or the asset is realised. Deferred tax is charged or credited to the consolidated income statement, except when it relates to items charged or credited directly to equity, in which case the deferred tax is also dealt with in equity.

Foreign currencies

In preparing the financial statements of each individual group entity, transactions in currencies other than the functional currency of that entity (foreign currencies) are recorded in the respective functional currency (i.e. the currency of the primary economic environment in which the entity operates) at the rates of exchanges prevailing on the dates of the transactions. At each balance sheet date, monetary items denominated in foreign currencies are retranslated at the rates prevailing on the balance sheet date. Non-monetary items carried at fair value that are denominated in foreign currencies are retranslated at the rates prevailing on the date when the fair value was determined. Non-monetary items that are measured in terms of historical cost in a foreign currency are not retranslated.

3. SIGNIFICANT ACCOUNTING POLICIES *(continued)*

Foreign currencies *(continued)*

Exchange differences arising on the settlement of monetary items, and on the translation of monetary items, are recognised in profit or loss in the period in which they arise. Exchange differences arising on the retranslation of non-monetary items carried at fair value are included in profit or loss for the period.

Leases

Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating leases.

Rental payable under operating leases are charged to the consolidated income statement on a straight line basis over the period of the leases.

4. KEY SOURCES OF ESTIMATION UNCERTAINTY

The following are the key assumptions concerning the future, and other key sources of estimation uncertainty at the balance sheet date, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year.

Estimated impairment of goodwill

Determining whether goodwill is impaired requires an estimation of the value in use of the cash-generating units to which goodwill has been allocated. The value in use calculation requires the Group to estimate the future cash flows expected to arise from the cash-generating unit and a suitable discount rate in order to calculate the present value. As at 31 December 2007, the carrying amount of goodwill is RMB58,479,000 (2006: RMB58,479,000). Details of the recoverable amount calculation are disclosed in note 16. Changes in estimation of the value in use would materially affect the carrying amounts of goodwill in the consolidated balance sheet and might give rise to impairment loss recognised in respect of goodwill in the consolidated income statement.

5. CAPITAL RISK MANAGEMENT

The Group manages its capital to ensure that entities in the Group will be able to continue as a going concern while maximising the return to shareholders through the optimisation of the debt and equity balance. The Group's overall strategy remains unchanged from prior year.

The capital structure of the Group consists of equity attributable to equity holders of the Company, comprising issued share capital and reserves including accumulated profits.

The directors of the Company review the capital structure on a semi-annual basis. As part of this review, the directors consider the cost of capital and the risks associates with each class of capital. Based on recommendations of the directors of the Company, the Group will balance its overall capital structure through the payment of dividends.

6. FINANCIAL INSTRUMENTS

Categories of financial instruments

	2007 **RMB'000**	2006 RMB'000
Financial assets		
Loans and receivables (including cash and cash equivalents)	**1,954,541**	1,670,001
Financial liabilities		
Amortised cost	**223,466**	148,885

Financial risk management objectives and polices

The Group's major financial instruments include bills and trade receivables, other receivables, trade and other payables. Details of the financial instruments are disclosed in respective notes. The risks associated with these financial instruments include market risk (foreign currency risk, fair value interest rate risk and other price risk), credit risk and liquidity risk. The policies on how to mitigate these risks are set out below. The management manages and monitors these exposures to ensure appropriate measures are implemented on a timely and effective manner.

Market risk

Foreign currency risk

Several subsidiaries of the Company have foreign currency bank balances, which expose the Group to foreign currency risk. Approximately 30% of the Group's bank balances are denominated in currencies other than the functional currency of the group entity.

6. FINANCIAL INSTRUMENTS *(continued)*

Market risk *(continued)*

Sensitivity analysis

The Group is mainly exposed to the currencies of HKD and USD with the functional currency of those subsidiaries in RMB. The following table details the Group's sensitivity to a 5% increase and decrease in RMB against the relevant foreign currencies. 5% is the sensitivity rate used which represents management's assessment of the reasonably possible change in foreign exchange rates. The sensitivity analysis includes only outstanding foreign currency denominated monetary items and adjusts their translation at the year end for a 5% change in foreign currency rates. A negative number below indicates a decrease in profit for the year where RMB strengthens 5% against the relevant currencies. For a 5% weakening of RMB against the relevant currencies, there would be an equal and opposite impact on the profit for the year.

	HKD Impact		**USD Impact**	
	2007	2006	**2007**	2006
	RMB'000	RMB'000	**RMB'000**	RMB'000
Decrease in profit for the year	**(12,544)**	(40,459)	**(14,016)**	(8)

Fair value interest rate risk

Interest bearing financial assets are mainly bank balances which are all short-term in nature and carry fixed interest rates. Therefore, the Group is not exposed to significant fair value interest rate risk due to the short maturity of financial assets. The Group currently does not have an interest rate hedging policy and will consider enter into interest rate hedging should the need rise.

Other price risk

The Group is exposed to equity price risk through its investments in listed equity securities. The management manages this exposure by maintaining a portfolio of investments with different risks. The Group's equity price risk is mainly concentrated on equity instruments operating in different industry sectors quoted in the Shanghai Stock Exchange. In addition, the Group has appointed a special team to monitor the price risk and will consider hedging the risk exposure should the need arise. The Group has disposed of those investments before year end.

6. FINANCIAL INSTRUMENTS *(continued)*

Credit risk

The Group's principal financial assets are bills and trade receivables, other receivables and bank balances. The maximum exposure to credit risk in the event that the counter parties fail to perform their obligations as at end of financial year in relation to each class of recognised financial assets is the carrying amount of those assets as stated in the consolidated balance sheet.

In order to minimise the credit risk, the management of the Group has delegated a team responsible for determination of credit limits, credit approvals and other monitoring procedures to ensure that follow-up action is taken to recover overdue debts. In addition, the Group reviews the recoverable amount of each individual trade and other receivables at each balance sheet date to ensure that adequate impairment losses are made for irrecoverable amounts. In this regard, the directors of the Company consider that the Group's credit risk is significantly reduced.

The credit risk on liquid funds is limited because majority of the counterparties are stateowned banks with good reputation.

The Group's concentration of credit risk by geographical locations is mainly in the People's Republic of China ("PRC"), which accounted for 97% (2006: 92%) of the total trade receivables as at 31 December 2007.

Liquidity risk

The directors of the Company has built an appropriate liquidity risk management framework for the management of the Group's short, medium and long-term funding and liquidity management requirements. The Group manages liquidity risk by continuously monitoring forecasted and actual cash flows and matching the maturity profiles of financial assets and liabilities. In the past, the Group relied on the funding generated from its operation.

The Group manages its liquidity by matching maturity profiles of financial assets and liabilities. The earliest date on which the Group can be required to pay the financial liabilities is less than 6 months from the respective balance sheet date while the Group expects to recover all the financial assets within 6 months from the respective balance sheet date.

6. FINANCIAL INSTRUMENTS *(continued)*

Liquidity risk *(continued)*

Fair value

The fair value of financial assets and financial liabilities are determined as follows:

- the fair value of financial assets with standard terms and conditions and traded on active liquid markets are determined with reference to quoted market bid prices; and

- the fair value of other financial assets and financial liabilities are determined in accordance with generally accepted pricing models based on discounted cash flow analysis using prices or rates from observable current market transactions as input.

The directors of the Company consider that the carrying amounts of financial assets and financial liabilities recorded at amortised cost approximate their fair values.

7. TURNOVER AND SEGMENT INFORMATION

Turnover represents the net amount received and receivable from sales of Chinese pharmaceutical products.

The Group's operation is regarded as a single segment, being an enterprise engaged in research and development, manufacture and trading of Chinese pharmaceutical products. Over 90% of the Group's sales are made in the PRC and over 90% of the Group's assets are situated in the PRC during the year. Accordingly, no segmental analysis of business and geographical segments is presented for the year.

8. INVESTMENT INCOME

	2007 **RMB'000**	2006 RMB'000
Interest on bank deposits	**38,340**	44,779
Dividends from held-for-trading investments	**2,213**	–
Net gain from held-for-trading investments	**166,688**	–
	207,241	44,779

Investment income earned on financial assets, analysed by category of asset, is as follows:

	2007 **RMB'000**	2006 RMB'000
Held-for-trading investments	**168,901**	–
Loans and receivables (including cash and bank balances)	**38,340**	44,779
	207,241	44,779

During the year ended 31 December 2007, the Group disposed all held-for-trading investments.

9. PROFIT BEFORE TAXATION

	2007 **RMB'000**	2006 RMB'000
Profit before taxation has been arrived at after charging:		
Auditor's remuneration	**1,822**	1,706
Cost of inventories recognised as expense	**212,615**	200,610
Depreciation of property, plant and equipment	**32,084**	29,733
Operating lease rentals in respect of land use rights	**675**	328
Staff costs (including directors' remuneration (see note 10))	**56,704**	51,347
Pension costs	**5,579**	3,064
Minimum lease payments under operating lease in respect of rented premises	**2,202**	1,714
Research and development costs	**4,930**	3,856
and after crediting:		
Government subsidies received (included in other income) (Note)	**23,990**	–
Gain on disposal of property, plant and equipment	**–**	28
Net exchange gain	**–**	756
Reversal of allowance for bad and doubtful debts	**–**	33

Note: It mainly represented the incentives received from PRC government for investments in relevant regions in the PRC by the Group.

10. DIRECTORS', SUPERVISORS' AND EMPLOYEES' REMUNERATION

Directors' remuneration:

Year ended 31 December 2007

	Fees RMB'000	Salaries, allowance and other benefits RMB'000	Pension costs RMB'000	Performance related incentive payments RMB'000	Total remuneration RMB'000
Name of executive directors:					
Li Zhenjiang	48	1,460	–	–	1,508
Wang Zhihua	48	639	–	–	687
Xin Yunxia	48	639	–	–	687
Li Huimin	48	662	–	53	763
Hung Randy King Kuen	48	1,313	12	67	1,440
Name of independent non-executive directors:					
Li Kung Man	115	–	–	–	115
Cheng Li	115	–	–	–	115
Ren Dequan	115	–	–	–	115
	585	4,713	12	120	5,430

10. DIRECTORS', SUPERVISORS' AND EMPLOYEES' REMUNERATION *(continued)*

Year ended 31 December 2006

	Fees RMB'000	Salaries, allowance and other benefits RMB'000	Pension costs RMB'000	Performance related incentive payments RMB'000	Total remuneration RMB'000
Name of executive directors:					
Li Zhenjiang	50	1,537	–	–	1,587
Wang Zhihua	50	673	–	–	723
Xin Yunxia	50	673	–	–	723
Li Huimin	50	700	–	–	750
Hung Randy King Kuen	50	1,382	12	91	1,535
Name of independent non-executive directors:					
Ren Dequan	60	–	–	–	60
Li Kung Man	121	–	–	–	121
Cheng Li	60	–	–	–	60
Wang Jianping	61	–	–	–	61
Zhou Chaofan	61	–	–	–	61
	613	4,965	12	91	5,681

10. DIRECTORS', SUPERVISORS' AND EMPLOYEES' REMUNERATION *(continued)*

Employees' remuneration:

The five highest paid individuals of the Group included 4 directors for the year (2006: 5), details of whose remuneration are set out above. The remuneration of the remaining 1 employee for the year (2006: Nil) is as follows:

	2007 **RMB'000**	2006 RMB'000
Salaries, allowance and other benefits	**1,843**	–
Pension costs	**92**	–
	1,935	–

Emoluments of these directors and employees were within the following bands:

	2007 **Number of** **Directors**	 **Employees**	2006 Number of Directors	 Employees
RMB500,001–RMB1,000,000	**2**	**–**	3	–
RMB1,000,001–RMB1,500,000	**1**	**–**	–	–
RMB1,500,001–RMB2,000,000	**1**	**1**	2	–
	4	**1**	5	–

During the year, no remuneration was paid by the Group to the directors or supervisors as an inducement to join or upon joining the Group or as compensation for loss of office. None of the directors and supervisors has waived any remuneration during the year.

The remuneration of directors and key executives is determined by the remuneration committee having regard to the performance of individuals and market trends.

11. INCOME TAX

	2007 **RMB'000**	2006 RMB'000
Current tax:		
PRC Enterprise Income Tax	**(83,431)**	(51,796)
Deferred tax expense (note 17)		
Current year	**1**	(2,261)
Attributable to a change in tax rate	**(1,870)**	–
	(1,869)	(2,261)
	(85,300)	(54,057)

The provision for PRC Enterprise Income Tax ("PRC EIT") is calculated based on the estimated taxable income for PRC taxation purposes at the rate of taxation applicable for the year.

11. INCOME TAX *(continued)*

The reconciliation of tax charge to the profit before taxation per the income statement for the year is as follows:

	2007		2006	
	RMB'000	**%**	RMB'000	%
Profit before taxation	**575,941**		387,034	
Tax at the applicable tax rate of 33%	**(190,061)**	**(33.0)**	(127,722)	(33.0)
Tax effect of expenses that are not deductible in determining taxable profit	**(22,880)**	**(4.0)**	(2,649)	(0.7)
Tax effect of income that are not taxable in determining taxable profit	**18,803**	**3.3**	6,814	1.8
Tax loss not recognised	**(2,226)**	**(0.4)**	(657)	(0.2)
Tax effect on tax exemption	**5,355**	**0.9**	54,395	14.1
Income tax on concessionary rate	**107,750**	**18.7**	13,460	3.5
Effect of different tax rates of subsidiaries operating in other jurisdiction	**–**	**–**	2,179	0.5
Decrease in opening deferred tax asset resulting from a decrease in applicable tax rate	**(1,870)**	**(0.3)**	–	–
Others	**(171)**	**(0.0)**	123	0.0
Taxation charge and effective tax rate for the year	**(85,300)**	**(14.8)**	(54,057)	(14.0)

On 16 March 2007, the PRC promulgated the Law of the People's Republic of China on Enterprise Income Tax (the "New Law") by Order No. 63 of the President of the PRC. On 6 December 2007, the State Council of the PRC issued Implementation Regulations of the New Law. The New Law and Implementation Regulations will change the tax rate from 33% to 25% for certain subsidiaries from 1 January 2008. The deferred tax balance has been adjusted to reflect the tax rates that are expected to apply to the respective periods when the asset is realised or the liability is settled.

Pursuant to the relevant law and regulations in the PRC, Shineway Pharmaceutical Co., Ltd. ("Shineway Pharmaceutical") and Hebei Shineway Pharmaceutical Co., Ltd. ("Hebei Shineway") are entitled to a 50% relief from PRC EIT for current year and the following year. The first profit-making period of Shineway Pharmaceutical and Hebei Shineway commenced on 1 January 2004 and the full exemption from PRC EIT ended on 31 December 2005.

11. INCOME TAX *(continued)*

Pursuant to 國發 1988 26號, the PRC EIT rate applicable to Shineway Sales is 15% on its assessable profit.

Pursuant to the 藏財税字 (94) 117號, Xizang Shineway Pharmaceutical Co., Ltd. ("Xizang Shineway") was exempted from the PRC EIT for the period from 21 May 2007 to 20 May 2008. Pursuant to 西藏拉薩經濟技術開發區優惠政策, the PRC EIT rate applicable to Xizang Shineway is 10% on its assessable profit.

Pursuant to 國發1988 26號, the PRC EIT rate applicable to Shineway Pharmaceutical (Hainan) Co., Limited ("Hainan Shineway") is 15% on its assessable profit.

12. EARNINGS PER SHARE

The calculation of the basic earnings per share is based on the following data:

	2007 **RMB'000**	2006 RMB'000
Earnings for the purposes of basic earnings per share	**490,641**	332,977

	Number of ordinary shares	
	2007	2006
Number of ordinary shares for the purposes of basic earnings per share	**827,000,000**	827,000,000

No diluted earnings per share is presented, as the Company did not have any potential ordinary shares outstanding.

13. DIVIDENDS

	2007 RMB'000	2006 RMB'000
Dividends recognised as distribution during the year		
Final dividend paid for 2006 of RMB10 cents (2005: RMB10 cents) per share	**82,700**	82,700
Special dividend paid for 2006 of RMB2 cents (2005: RMB2 cents) per share	**16,540**	16,540
Interim dividend paid for 2007 of RMB11 cents (2006: RMB10 cents) per share	**90,970**	82,700
	190,210	181,940
Dividends proposed		
Proposed final dividend of RMB11 cents (2006: RMB10 cents) per share	**90,970**	82,700
Proposed special dividend of RMB16 cents (2006: RMB2 cents) per share	**132,320**	16,540
	223,290	99,240

The dividends will be paid to the shareholders of the Company whose names appear on the Register of Members on 28 April 2008.

14. PROPERTY, PLANT AND EQUIPMENT

	Buildings RMB'000	Plant and machinery RMB'000	Office equipment RMB'000	Motor vehicles RMB'000	Construction in progress RMB'000	Total RMB'000
COST						
At 1 January 2006	149,750	166,624	7,131	1,589	17,950	343,044
Additions	–	4,483	1,151	822	16,763	23,219
Reclassifications	15,722	10,304	485	–	(26,511)	–
Disposals	–	(326)	(3)	(47)	–	(376)
Currency realignment	–	–	(32)	–	–	(32)
At 1 January 2007	165,472	181,085	8,732	2,364	8,202	365,855
Additions	–	18,468	4,303	311	63,243	86,325
Reclassifications	29,469	29,056	2,178	–	(60,703)	–
Currency realignment	–	–	(118)	–	–	(118)
At 31 December 2007	**194,941**	**228,609**	**15,095**	**2,675**	**10,742**	**452,062**
DEPRECIATION						
At 1 January 2006	30,415	79,077	2,241	118	–	111,851
Provided for the year	7,157	21,086	1,197	293	–	29,733
Reclassifications	–	(2)	2	–	–	–
Eliminated on disposals	–	(45)	(3)	(42)	–	(90)
Currency realignments	–	–	(7)	–	–	(7)
At 1 January 2007	37,572	100,116	3,430	369	–	141,487
Provided for the year	7,775	20,848	2,129	1,332	–	32,084
Currency realignments	–	–	(56)	–	–	(56)
At 31 December 2007	**45,347**	**120,964**	**5,503**	**1,701**	**–**	**173,515**
CARRYING VALUES						
At 31 December 2007	**149,594**	**107,645**	**9,592**	**974**	**10,742**	**278,547**
At 31 December 2006	127,900	80,969	5,302	1,995	8,202	224,368

The following rates are used for the depreciation of property, plant and equipment:

Buildings	5%
Plant and machinery	10% – 33%
Office equipment	20%
Motor vehicles	33%

15. LAND USE RIGHTS

	2007 RMB'000	2006 RMB'000
CARRYING VALUE		
At 1 January	**5,946**	6,274
Addition during the year	**15,298**	–
Expense for the year	**(675)**	(328)
At 31 December	**20,569**	5,946
Analysed for reporting purposes as:		
Current portion (included in other receivables)	**675**	328
Non-current portion	**19,894**	5,618
	20,569	5,946

The amount represents the payment for medium term land use rights situated in the PRC, amortise over the periods ranging from 45 to 50 years.

16. GOODWILL

	RMB'000
At 1 January 2006, 1 January 2007 and 31 December 2007	58,479

For the purpose of impairment testing, goodwill has been allocated to one cash-generating unit ("CGU") including three subsidiaries with principal activity of trading Chinese pharmaceutical products. These three subsidiaries are Shineway Sales, Hainan Shineway and Xizang Shineway. During the year ended 31 December 2007, management of the Group determines that there are no impairments of its CGU containing goodwill.

16. GOODWILL *(continued)*

The basis of the recoverable amounts of the above CGU and their major underlying assumptions are summarised below:

The recoverable amount of the above CGU has been determined based on a value in use calculation. That calculation uses cash flow projections based on most recent financial budgets approved by management covering a ten-year period, and discount rate of 12% (2006: 8%), with an estimated constant growth rate of 6% which does not exceed the average long-term growth rate for the relevant markets. Other key assumptions for the value in use calculations relate to the estimation of cash inflows/outflows which include budgeted sales and gross margin, such estimation is based on the unit's past performance and management's expectations for the market development. Management believes that any reasonably possible change in any of these assumptions would not cause the aggregate carrying amount of CGU to exceed the aggregate recoverable amount of CGU.

17. DEFERRED TAXATION

The followings are the major deferred tax assets recognised and movement thereon during the year.

	Accelerated tax depreciation	**Others**	**Total**
	RMB'000	RMB'000	RMB'000
At 1 January 2006	7,327	4,132	11,459
Credited (charged) to consolidated income statement for the year	635	(2,896)	(2,261)
At 1 January 2007	7,962	1,236	9,198
Effect of change in tax rate	(1,870)	–	(1,870)
(Charged) credited to the consolidated income statement for the year	(146)	147	1
At 31 December 2007	**5,946**	**1,383**	**7,329**

At the balance sheet date, the Group has unused tax losses RMB17,845,000 (2006: RMB10,820,000) available for offset against future profits. No deferred tax asset has been recognised due to the unpredictability of future profit streams. The tax losses may be carried forward indefinitely.

18. INVENTORIES

	2007 RMB'000	2006 RMB'000
Raw materials	**31,803**	13,708
Work in progress	**21,486**	11,434
Finished goods	**25,063**	13,055
	78,352	38,197

All inventories were carried at cost at the respective balance sheet dates.

19. OTHER FINANCIAL ASSETS

	2007 RMB'000	2006 RMB'000
Bills receivables and trade receivables:		
Bills receivables	**244,820**	63,301
Trade receivables	**8,865**	3,346
	253,685	66,647

The Group allows a credit period normally ranging from six months to one year to its trade customers. The bills receivables and trade receivables are of the age within 6 months at the balance sheet dates.

Before accepting any new customer, the Group has appointed a special term to monitor the potential customer's credit quality and defines credit limits by customer, which are reviewed every year. More than 90% of the trade receivables are neither past due nor impaired.

Bank balances and cash comprises cash held by the Group and short-term bank deposits with an original maturity of three months or less. The effective interest rate ranged from 0.72% to 4.86% per annum in both years.

At the balance sheet date, certain bank balances and cash of RMB1,142,934,000 (2006: RMB774,993,000) were denominated in RMB which is not a freely convertible currency in the international market. The exchange rate of RMB is determined by the Government of the PRC and the remittance of these funds out of the PRC is subject to exchange restrictions imposed by the Government of the PRC.

19. OTHER FINANCIAL ASSETS *(continued)*

Included in bills receivables, trade and other receivables and bank balances are the following amounts denominated in currencies other than the functional currency of the relevant group entity to which they relate.

	2007 RMB'000	2006 RMB'000
Hong Kong Dollars	**264,076**	820,087
United States Dollars	**280,313**	158

20. PLEDGED ASSETS

Pledged assets represents certain bills receivable and bank deposits pledged to banks to secure banking facilities granted to the Group. As at 31 December 2006, bills receivables of RMB1,368,000 and bank deposits of RMB1,882,000 were pledged to bank to secure bills payables totalling RMB2,973,000 issued by the Group. The pledged assets were released upon the settlement of the relevant bills payables.

21. OTHER FINANCIAL LIABILITIES

	2007 RMB'000	2006 RMB'000
Bills payables	**–**	2,973
Trade payables	**89,172**	73,173
	89,172	76,146

An aged analysis of the Group's trade and bills payables at the balance sheet date is as follows:

	2007 RMB'000	2006 RMB'000
Within 6 months	**83,744**	71,214
Over 6 months but less than 1 year	**5,258**	3,724
Over 1 year but less than 2 years	**108**	1,198
Over 2 years	**62**	10
	89,172	76,146

21. OTHER FINANCIAL LIABILITIES *(continued)*

Trade payables principally comprise amounts outstanding for trade purchases and ongoing costs. The average credit period taken for trade purchase ranges from two months to six months.

Included in trade payables, bills payable and receipt in advance are the following amounts denominated in currency other than the functional currency of the entity.

	2007	2006
	RMB'000	RMB'000
Hong Kong Dollars	**5,248**	8,943

22. AMOUNTS DUE TO RELATED COMPANIES

	2007	2006
	RMB'000	RMB'000
Shineway Medical Science & Technology (Lang Fang) Co., Ltd. ("Shineway Lang Fang")	**9,594**	587
Shineway Medical Science & Technology Co., Ltd. ("Shineway Medical")	**469**	–
	10,063	587

The amounts due to related companies as at 31 December 2007 are unsecured, interest-free and repayable on demand.

23. GOVERNMENT GRANTS RECEIVED

The amounts represent government subsidies received in advance in relation to research and development expenses on certain new products. The amounts are recognised in the same period as the related research and development expenses are incurred and are deducted in reporting the related research and development expenses. The grant is recognised as deferred income because there is an obligation to repay the grant if the related research is not successfully completed.

24. SHARE CAPITAL

	Number of shares '000	Amount RMB'000
Ordinary shares of HK$0.10 each		
Authorised:		
Balance at 31 December 2006 and 31 December 2007	5,000,000	530,000
Issued and fully paid:		
Balance at 31 December 2006 and 31 December 2007	827,000	87,662

25. SHARE OPTIONS

The Company's share option scheme (the "Scheme"), was adopted pursuant to a resolution passed on 10 November 2004 for the primary purpose of providing incentives to:

(a) director or employee of any members of the Group;

(b) any discretionary object of a discretionary trust established by any substantial shareholder of the Company or employee of any member of the Group;

(c) any consultant, professional and other advisers to any member of the Group;

(d) any chief executive or substantial shareholder of any member of the Group;

(e) any associate of any director, chief executive or substantial shareholder of any member of the Group; and

(f) any employee (whether full-time or part-time) of substantial shareholder of any member of the Group to take up options.

The Scheme will expire on 9 November 2014. Under the Scheme, the Board of Directors of the Company may grant options to eligible person to subscribe for shares in the Company.

25. SHARE OPTIONS *(continued)*

The total number of shares in respect of which options may be granted under the Scheme is not permitted to exceed 10% of the shares of the Company in issue at any point of time, without prior approval from the Company's shareholders. The number of shares issued and to be issued in respect of which options granted and may be granted to any individual in any one year is not permitted to exceed 1% of the shares of the Company in issue at any point in time, without prior approval from the Company's shareholders. Options granted to substantial shareholders, independent non-executive directors, or any of their respective associates (including a discretionary trust whose discretionary objects include a substantial shareholder or an independent non-executive director or a company beneficially owned by any substantial shareholder or independent non-executive director of the Company) in excess of 0.1% of the Company's share capital or with a value in excess of HK$5,000,000 must be approved in advance by the Company's shareholders.

Option granted must be taken up within 14 days from the date of offer, upon payment of HK$1 per option. Options may be exercise at any time from the date of grant of the share option to the 10 anniversary of the date of grant. The exercise price is determined by the directors of the Company, and will not be less than the higher of (i) the closing price of the Company's shares on the date of grants; (ii) the average closing price of the shares for the five business days immediately preceding the date of grant; and (iii) the nominal value of the Company's share.

No option has been granted since adoption.

26. RESERVES

(a) Basis of appropriations to reserves

The transfers to statutory surplus reserve fund, statutory public welfare fund and discretionary surplus reserve fund are based on the profit in the financial statements prepared under Chinese Accounting Standards.

(b) Statutory surplus reserve fund

Shineway Pharmaceutical, Hebei Shineway and Shineway Sales's Articles of Association ("Articles") require the appropriation of 10% of its profit after taxation each year to the statutory surplus reserve fund until the balance reaches 50% of the registered share capital. According to the provision of the Articles, in normal circumstances, the statutory surplus reserve fund shall only be used for making up losses, capitalisation into share capital and expansion of production and operation. For the capitalisation of statutory surplus reserve fund into share capital, the remaining amount of such reserve fund shall not be less than 25% of the registered share capital.

26. RESERVES *(continued)*

(b) Statutory surplus reserve fund *(continued)*

During the year ended 31 December 2007, Shineway Pharmaceutical, Hebei Shineway, Shineway Sales, Hainan Shineway and Xizang Shineway amended the appropriation percentage from 10% to 15% by passing ordinary resolution at the Board of Directors' meetings.

(c) Statutory public welfare fund

Pursuant to the PRC Company Law, Shineway Pharmaceutical, Hebei Shineway, Shineway Sales's shall make allocation from its profit after taxation at the rate of 5% to 10% to the statutory public welfare fund. The statutory public welfare fund can only be utilised on capital items for employees collective welfare. Individual employees only have the right to use these facilities, the titles to which will remain with Shineway Pharmaceutical, Hebei Shineway and Shineway Sales. The statutory public welfare fund forms part of the shareholders' equity but is not distributable other than in liquidation.

Pursuant to a circular issued by Ministry of Finance, there will be no appropriation of statutory public welfare fund started from 1 January 2006. The remaining balance of such fund is transferred to statutory surplus reserve fund.

(d) Discretionary surplus reserve fund

Pursuant to the Articles, Shineway Pharmaceutical, Hebei Shineway, Shineway Sales, Hainan Shineway and Xizang Shineway shall make allocation from its profit after taxation and appropriations to the discretionary surplus reserve fund at the rate decided by the shareholders annually. In normal circumstances, the discretionary surplus reserve fund shall only be used for making up losses, capitalisation into share capital and expansion of Shineway Pharmaceutical, Hebei Shineway, Shineway Sales, Shineway Hainan and Xizang Shineway's production and operation.

(e) Merger reserve

Merger reserve of the Group represents the difference between the net asset value of Yuan Da International Limited ("Yuan Da") and Hong Zhan International Limited ("Hong Zhan") and the nominal amount of the Company's shares which were issued as consideration for the acquisition of Yuan Da and Hong Zhan at the time of the group reorganisation in 2004.

27. OPERATING LEASE

At the balance sheet date, the Group had commitments for future minimum lease payments under non-cancellable operating lease which fall due as follows:

	2007 RMB'000	2006 RMB'000
Within one year	**1,729**	1,211
In the second to fifth year inclusive	**2,351**	391
	4,080	1,602

Operating lease payments represent rentals payable by the Group for certain of its warehouse, staff quarters and offices. Leases are negotiated for terms ranged from 1 to 3 years with fixed rental.

Included in the operating lease commitment, RMB352,000 (2006: RMB469,000) as fall due within one year and nil (2006: RMB352,000) fall due in the second to fifth year inclusive are payable to Shineway Medical.

28. RETIREMENT BENEFITS PLANS

The employees of the Group participate in retirement and medicare insurances in accordance with the PRC laws and related regulations. When an employee joins the Group, he is enrolled with the local retirement plan. Contributions to the retirement insurance, borne by the Group and the employee jointly at the proportions stipulated by the local Municipal Government, are paid to the social insurance institutions monthly. When the employee retires, he receives his retirement funds from the insurance company directly and is also entitled to enjoy medical benefits after retirement provided by the insurance company. Other than this, the Group has no obligation for any related retirement benefits.

The total expense recognised in the consolidated income statement of RMB5,579,000 (2006: RMB3,064,000) represents contributions payable to this plan by the Group at rates specified in the rules of the plan.

29. CAPITAL COMMITMENTS

	2007 RMB'000	2006 RMB'000
Capital expenditure in respect of acquisition of property, plant and equipment contracted for but not provided in the consolidated financial statements	**8,756**	2,545

30. RELATED PARTY TRANSACTIONS

During the year, the Group had the following significant transactions with related parties:

	2007 RMB'000	2006 RMB'000
Trading transactions:		
Rental expenditure paid to Shineway Medical (note a)	**469**	469
Service fee to Shineway Lang Fang (note b)	**1,174**	1,174
Service fee to Shineway Medical (note a)	**6,955**	6,955
Sale of goods to Shineway Drugstores (note a)	**–**	277
Purchase from Shineway Lang Fang (note b)		
– Research & Development Centre	**8,662**	–
– Related land use rights	**15,298**	–

Notes:

(a) Shineway Medical, which is owned by the beneficial shareholder of the Company, holds 80% equity interest in Shineway Drugstore.

(b) Shineway Medical owns 70% equity interest in Shineway Lang Fang.

31. SUBSIDIARIES

Details of the subsidiaries at 31 December 2007 are as follows:

Name of company	Place and date of incorporation/ establishment	Issued and fully paid/ registered capital	Percentage of equity interest held by the Company Directly	Indirectly	Principal activities
Yuan Da 遠大國際有限公司	British Virgin Islands ("BVI") 20 November 2002	Share – US$10,000	100%	–	Investment holding
Hong Zhan 宏展國際有限公司	BVI 20 November 2002	Share – US$10,000	100%	–	Investment holding
Shineway Sales 神威藥業營銷有限公司 (Note a)	PRC 3 March 2003 for a term of 30 years	Registered capital – RMB98,533,542	–	100%	Trading of Chinese pharmaceutical products
Shineway Pharmaceutical 神威藥業有限公司 (Note b)	PRC 30 December 2003 for a term of 30 years	Registered capital – US$25,000,000	–	100%	Research and development, manufacture and trading of Chinese pharmaceutical products
Hebei Shineway 河北神威藥業有限公司 (Note b)	PRC 30 December 2003 for a term of 30 years	Registered capital – US$12,000,000	–	100%	Manufacture and trading of Chinese pharmaceutical products
China Shineway Pharmaceutical (Hong Kong) Limited 中國神威藥業(香港)有限公司	Hong Kong 21 April 2004	Share – HK$1	–	100%	Trading of Chinese pharmaceutical products

31. SUBSIDIARIES *(continued)*

Name of company	Place and date of incorporation/ establishment	Issued and fully paid/ registered capital	Percentage of equity interest held by the Company Directly	Indirectly	Principal activities
Xizang Shineway 西藏神威藥業有限公司 (Note b)	PRC 7 November 2006 for a term of 10 years	Registered capital – US$1,250,000	–	100%	Trading of Chinese pharmaceutical products
Hainan Shineway 神威藥業(海南)有限公司 (Note b)	PRC 21 May 2007 for a term of 10 years	Registered capital – US$3,900,000	–	100%	Trading of Chinese pharmaceutical products

Notes:

(a) With effect from 30 March 2005, Shineway Sales has become a foreign wholly-owned enterprise after the equity interest transfer.

(b) Shineway Pharmaceutical, Hebei Shineway, Xizang Shineway and Hainan Shineway are foreign wholly-owned enterprises.