BUSINESS

OVERVIEW

We are the largest distributor of, and a leading provider of supply chain services for, pharmaceutical and healthcare products and operate the largest national pharmaceutical distribution network in China, based on our revenues in 2008 and according to China Association of Pharmaceutical Commerce, or CAPC. We have been able to rapidly grow our market share and profits in a highly fragmented industry by taking advantage of our economies of scale and nationwide distribution network, through which we offer a range of value-added supply chain services for our customers and suppliers. According to CAPC, our market share, measured as a percentage of the total revenues of pharmaceutical distributors in China, increased from approximately 4.4% in 2003 to 10.8% in 2008. According to CAPC, we have also increased our lead in terms of market share over our nearest competitor from less than 0.1% in 2003 to 6.1% in 2008.

We have integrated operations in the following business segments, namely:

- *Pharmaceutical distribution.* Pharmaceutical distribution is our principal business. We provide distribution, logistics and other value-added services for pharmaceutical and healthcare products of domestic and international manufacturers and other suppliers. We differentiate ourselves from our competitors in China by our geographic coverage, the breadth of our product portfolio and the strength of the supply chain services we provide to our customers and suppliers.

- *Retail pharmacy.* We have a network of retail drug stores that we directly operate or franchise in major cities throughout China. Our retail pharmacy operations contributed less than 5% of our total revenues in the three years ended 31 December 2006, 2007 and 2008 and the five months ended 31 May 2009.

- *Other business operations.* We are also engaged in the manufacturing or selling of pharmaceutical products, chemical reagents and laboratory supplies. Our other business operations contributed less than 5% of our total revenues in the three years ended 31 December 2006, 2007 and 2008 and the five months ended 31 May 2009.

We operate in a fast-growing and highly fragmented industry. According to CAPC, the pharmaceutical distribution industry in China grew at a CAGR of approximately 16% from 2003 to 2008, which we believe was driven by favorable socio-economic factors and strong government support. Furthermore, the PRC Government has recently announced a reform plan to spend RMB850 billion on healthcare, which is in addition to the regular healthcare budget, from 2009 to 2011 in order to increase the availability of healthcare, basic medicines and health insurance coverage in China. As a comparison, in 2007, the total healthcare expenditure in China was approximately RMB1.1 trillion, of which approximately RMB230 billion was government spending, according to the Ministry of Health. The healthcare reform plan is expected to accelerate growth in the PRC pharmaceutical industry. In addition, the highly fragmented pharmaceutical distribution industry has recently commenced a process of consolidation, which has led to an increase in market share of the three largest pharmaceutical distributors from 12.7% in 2003 to 20.0% in 2008, according to CAPC, and the healthcare reform plan is expected to contribute to further consolidation.

We believe that we are well-positioned to benefit from the healthcare reform plan and PRC pharmaceutical industry trends, and add to our leading market position in China. With our

geographically diverse distribution network of 25 distribution centers, spanning 19 provinces, municipalities and autonomous regions in China, we are able to provide our products and services to our customers across China in a timely and cost-effective manner. In particular, in 2008, over 80% of pharmaceutical sales in China were made at hospital pharmacies, rather than at unaffiliated retail pharmacies, and we sold, directly or indirectly through our distributor customers, our pharmaceutical and healthcare products to hospitals in every region and province of China. As of 31 May 2009, our direct customers included approximately 36.4% of all hospitals in China, encompassing 56.2% of the largest, most highly ranked class-three hospitals, and over 24,000 other customers, such as pharmaceutical distributors, retail pharmacies and other healthcare institutions. The following table sets forth a breakdown of our direct customers in our pharmaceutical distribution segment as of 31 May 2009:

	Number
Hospitals	4,723
Distributor Customers	2,545
Retail Pharmacies and Other Customers	22,155

We focus on offering a comprehensive range of products through our distribution network, which included over 22,000 different types of pharmaceutical and healthcare products as of 31 May 2009, comprising branded and generic prescription medicines and over-the-counter medicines, as well as personal care products and medical supplies. We source our products from over 3,300 domestic and international pharmaceutical companies, including 30 of the top 50 international pharmaceutical companies, such as Roche, AstraZeneca, Pfizer, GlaxoSmithKline, Merck, Eli Lilly, and Novo Nordisk, and 95 of the top 100 domestic pharmaceutical companies, such as Jiangsu Hengrui, Harbin Pharma and North China Pharma. As of the Latest Practicable Date, we distributed 46 of the 50 international top-selling pharmaceutical products, according to IMS statistics, in China. In addition, we are one of the only three licensed nationwide anesthetics distributors in China, and we currently hold approximately 90% of the PRC market share in this segment according to China Anesthetics Association.

As part of our pharmaceutical distribution operations, we offer a broad range of logistics and value-added services to our customers and suppliers that enable them to maintain and improve their performance. For example, our services benefit our hospital customers by helping them to improve the delivery of pharmaceutical and healthcare products to patients and lower their overall costs in the pharmaceutical supply chain. We are able to integrate our information management system with those of the hospitals, perform inventory tracking of medicines, which assists hospitals to maintain appropriate levels of inventory, and provide logistics services, ensuring medicines are delivered promptly and at reduced costs to customers. With respect to suppliers, our supply chain services ensure the quality and timely distribution of their products to multiple customers in all parts of China. See "Business — Pharmaceutical Distribution — Value-added Services". Our customers and suppliers value our ability to provide these services, which further enhances our relationships with them and strengthens our role as a leading supply chain services provider.

We have experienced significant growth in our business in recent years. Our revenues increased from RMB23,736.6 million in 2006 to RMB31,110.2 million in 2007 and to RMB38,187.4 million in 2008, representing a CAGR of 26.8% from 2006 to 2008. Our net profit, defined as after tax profit attributable to our equity holders, increased from RMB101.3 million in 2006, to RMB380.9 million in 2007 and to RMB585.7 million in 2008, representing a CAGR of 140.4% from 2006 to 2008. In the five months ended 31 May 2009, our revenue amounted to RMB18,048.0 million, representing an increase of 20.3% over the same period in 2008, and in the five months ended 31 May 2009, our net profit, defined as after tax profit attributable to our equity shareholders, amounted to RMB421.5 million, representing an increase of 41.9% over the same period in 2008. As we have

grown, our increased economies of scale and measures to improve our cost and operating efficiencies have allowed us to continue to improve our operating and net margins. Our operating margins were 2.0%, 2.5%, 3.1% and 3.9% in the years ended 31 December 2006, 2007 and 2008 and the five months ended 31 May 2009, respectively. In the same periods, our net margins were 0.4%, 1.2%, 1.5% and 2.3%, respectively.

OUR COMPETITIVE STRENGTHS

We are the industry leader in the distribution of pharmaceutical and healthcare products in China both in terms of our market share and the geographical range of our distribution network.

We are the largest and leading national distributor of pharmaceutical and healthcare products, and we operate the most expansive distribution network in China according to CAPC. Our industry standing has made us a preferred distributor for leading Chinese and international manufacturers and suppliers of pharmaceutical and other healthcare products. According to CAPC, we have been the largest distributor of pharmaceutical products in China since 2003, and we have steadily increased our lead in market share over our nearest competitor. According to CAPC, our market share, measured as a percentage of the total revenues of pharmaceutical distributors in China, was 10.8% in 2008, which is more than twice that of our nearest competitor and the largest overall in China.

As China's leading pharmaceutical distributor, we are well-positioned to benefit from the strong growth, consolidation, and regulatory reform in the PRC pharmaceutical and healthcare industry.

The PRC healthcare market is one of the fastest-growing healthcare markets in the world, driven by China's rapidly growing economy, rising living standards, increased health consciousness, large aging population and proactive government policies. Furthermore, the PRC Government recently announced a reform plan to spend RMB850 billion on healthcare in addition to the regular healthcare budget from 2009 to 2011, in order to increase the availability of healthcare, basic medicines and health insurance coverage for people in China. As a comparison, in 2007, the total healthcare expenditure in China was approximately RMB1.1 trillion, of which approximately RMB230 billion was government spending, according to the Ministry of Health. The healthcare reform plan is expected to accelerate growth in the PRC pharmaceutical industry not only by the increased government spending, but also by the expected increases in private healthcare spending stimulated by larger government subsidies to PRC residents, as per capita healthcare spending remains much lower than in developed countries. We are well-positioned to capture business opportunities resulting from this fast-growing market.

In addition, China's pharmaceutical distribution market is highly fragmented and is characterized by inefficient supply chains. The highly fragmented pharmaceutical distribution industry has recently commenced a process of consolidation, which has led to an increase in market share of the three largest pharmaceutical distributors, from 12.7% in 2003 to 20.0% in 2008. As was the case in the development of the currently mature U.S. and European pharmaceutical distribution markets, we expect the PRC pharmaceutical distribution market to continue to consolidate into one with larger and more efficient distributors. In addition, we expect the healthcare reform plan to promote further consolidation, as it calls for reducing the number of layers between manufacturers and consumers of medicines. We believe that we have the scale, industry standing, brand and financial strength to compete effectively during this process of consolidation.

The PRC Government has also adopted measures to raise the operating standards of pharmaceutical companies and promote the quality of distribution of pharmaceutical products in China, in order to ensure a stable supply of safe, effective medicines at reasonable prices. We believe we will

benefit from future regulatory reforms, which require pharmaceutical manufacturers and distributors to implement more stringent standards on the manufacturing and distribution of pharmaceutical products. Unlike smaller distributors, we have a large-scale distribution network, high quality equipment and facilities, leading management and qualified personnel, which are required to satisfy the higher standards. These attributes also provide us with a competitive edge over our competitors.

In addition to growing organically, we have also grown through acquisitions in a consolidating industry and possess significant experience in integrating acquired targets.

In addition to growing organically, through expanding our distribution network and increasing our sales volumes, we have also grown through acquisitions. We have achieved success in completing acquisitions of pharmaceutical companies in China. Through past successful acquisitions, we have demonstrated our ability to effectively integrate acquisition targets in different market segments and regions. We have seamlessly combined the resources and strengths of the acquired businesses with our existing operations. Since 2003, we have acquired several pharmaceutical distributors in China from independent third parties as part of our focus to expand our business operations in, and the geographic coverage of, our pharmaceutical distribution segment. Notable acquisitions include regional pharmaceutical distributors such as Accord Pharma, Sinopharm Suzhou, Sinopharm Henan, Sinopharm Hubei, Sinopharm Jiangsu, Sinopharm Hunan and Sinopharm Anhui. We offer acquisition targets a variety of benefits such as our extensive pharmaceutical distribution network, broad product portfolio, well-established brand name, full range of logistics services, our advanced operation model and information management system and economies of scale. We believe we have successfully integrated our past acquisition targets and such experience will enable us to capture and integrate additional opportunities that may arise, allowing us to continue growing our pharmaceutical distribution network and our business scale.

We believe we have the most competitive pharmaceutical distribution network in China, due to our broad geographic and market coverage, strong relationships with customers and suppliers, comprehensive logistics arrangements, advanced value-added supply chain services and infrastructure, and well-established "Sinopharm" brand name.

We believe the market leading position of our distribution network is due to the following factors, which provides us with a sustainable business advantage over existing and prospective competitors:

- *Broad geographic and market coverage*. We have a nationwide geographically diverse distribution network of 25 distribution centers, spanning 19 provinces, municipalities and autonomous regions in China. We also have a broad product portfolio of over 22,000 different types of pharmaceutical and healthcare products. We believe our distribution network and product portfolio is broader than those of our competitors.

- *Strong relationships with customers and suppliers.* As of 31 May 2009, we had contracts with 30 of the top 50 international and 95 of the top 100 domestic manufacturers of pharmaceutical and healthcare products and have established close business relationships with these leading manufacturers. We also enjoy strong relationships with our customers, often serving as one of the primary sources of pharmaceutical and healthcare products for them. We have a stable and diverse customer base, comprising hospitals, other distributors, retail drug stores and other entities that sell pharmaceutical and healthcare products, located throughout China. The breadth of our distribution network and product portfolio, and our advanced value-added and logistics services, which we believe to be limited to the leading distributors in China, strengthens our existing supplier and customer relationships, allows us to respond quickly and efficiently to our customers' pharmaceutical requirements and enables us to pursue new relationships with key pharmaceutical and healthcare product suppliers.

- *Comprehensive logistics arrangements.* We provide comprehensive logistics arrangements, consisting of storage, warehousing, and long-distance, regional and local transportation and delivery services through our well-established and improving logistics infrastructure. Our logistics arrangements aim to manage the flow of products and information with high efficiency and precision, as well as minimize our inventory holding costs.

- *Advanced value-added supply chain services.* We provide advanced value-added supply chain services, such as supplier solutions, online product ordering, inventory tracking and management, distribution center management and supply chain management consulting. Our value-added services benefit our customers by improving the delivery of pharmaceutical and healthcare products to patients, lowering their overall costs in the pharmaceutical supply chain, and benefit our suppliers by ensuring the quality and timely distribution of their products and meeting their needs for operational flexibility, efficiency and cost-effectiveness. We believe the strength of our advanced value-added supply chain services differentiates ourselves from our competitors.

- *Well established brand name.* As a result of our leading market position, consistent high service quality and commitment to provide superior services, the "Sinopharm" brand is widely recognized. We believe that the well established "Sinopharm" brand name plays an important role in our ability to maintain and enhance strong relationships with our suppliers and customers and contributes to the strength of our distribution network.

We believe these factors constitute a competitive advantage, differentiate us from our competitors and allow us to achieve and benefit from economies of scale and operating efficiencies.

We continue to increase operational and cost efficiencies due to our economies of scale, integrated logistics systems and modern information management systems.

Our distribution network and large-scale operations offer us enhanced operational and cost efficiencies and position us favorably against other distributors in China's highly fragmented pharmaceutical distribution market. In particular, our senior management, recognizing that controlling costs is an important aspect of operational efficiency, has focused a significant amount of its attention on reducing our cost structure. Our distribution and selling expenses and general and administrative expenses as a percentage of our total revenue decreased from 6.4% in 2006, to 5.1% in 2008 and to 4.2% in the five months ended 31 May 2009. As a result, our operating margins increased from 2.0% in 2006, to 3.1% in 2008 and to 3.9% in the five months ended 31 May 2009 and our net margins increased from 0.4% in 2006, to 1.5% in 2008 and to 2.3% in the five months ended 31 May 2009.

We place particular emphasis on integrating our logistics systems and information management systems with the consistent expansion of our services and products to operate cost-competitively and to increase our profitability. In order to further increase our operational efficiencies, we have implemented chain management and warehouse management solutions systems. These information management systems allow us to provide services spanning the entire pharmaceutical supply chain in a timely, cost-effective and efficient manner. At the same time, we are able to increase the precision of our inventory control systems and enhance the planning of our logistics resources with our integrated logistics systems. We are committed to establish uniform and computerized information management systems to improve our financial risk management and to oversee our overall capital investments, financial accounting and business operations. These systems also allow us to share consolidated sales and marketing information with our suppliers and customers. We view the continuing improvement of our logistics and information management systems as critical to our future profitability, growth and cost competitiveness. These systems also provide us with a competitive edge over our competitors.

We have an experienced and committed professional management team and highly-qualified employees.

We are led by a strong team of highly experienced professionals in the fields of pharmaceutical supply chain management. The majority of our senior management team possesses an average of 15 years of related experience. Many of our directors and senior management are elected to serve as high-ranking officers of various major pharmaceutical industry and trade organizations, such as CAPC, China Anesthetics Association, China Pharmaceutical Entrepreneur Association and China Pharmaceutical Enterprises Management Association, and have the opportunity to participate and advise on industry policy initiatives. Our strong management team has extensive experience in mergers and acquisitions in the pharmaceutical and healthcare industry, and has been active in capturing market opportunities, forming and implementing successful business strategies, assessing and managing risks, directing our expansion efforts to high growth areas and increasing our overall profitability. We believe that we have the requisite leadership to continue to build upon our core strengths to execute our business strategies.

OUR BUSINESS STRATEGIES

Our objectives are to consolidate our position as the top distributor of, and supply chain services provider for, pharmaceutical and healthcare products in China and continue to grow and play a significant role in the development of the pharmaceutical and healthcare industry in China. We aim to achieve these objectives through the following strategic initiatives:

Continue to expand our geographic reach and optimize our distribution operations, customer composition and product portfolio to add to our leading position in the pharmaceutical distribution industry.

We intend to continue to improve our operations, exploit our competitive strengths, and expand our operations to add to our leading position in the pharmaceutical distribution industry. We aim to extend our direct geographical reach in China through establishing new distribution centers or by completing acquisitions, with the goal of having a facility in every province and region in China, other than Tibet, in the next two years. We intend to bolster our direct selling efforts to hospitals, in order to build stronger relationships with these significant customers. We also expect to enhance our penetration into new customer categories and demographics. For example, we intend to continue to improve our relationships with hospitals in urban areas, community clinics at the provincial and municipal levels, and other customers in rural areas. We plan to optimize our pharmaceutical distribution operations by further centralizing our procurement, establishing standard operating procedures, consolidating our financial management system and logistics resources and enhancing our internal controls. We will also seek to optimize our product portfolio, include more products with higher margins, expand our service offerings and leverage our leading position in the distribution of anesthetics, vaccines and specialty medicines.

As we do so, we believe our greater sourcing capability and cost-efficiency will make us a more attractive distribution channel for many pharmaceutical and healthcare product manufacturers. Further, we intend to distinguish ourselves through the variety and depth of our products and value-added services, operational flexibility and rapid and responsive customer support that we can provide seamlessly to our customers. We also believe we can capitalize on significant market opportunities in the rapidly growing PRC pharmaceutical industry by expanding our existing market coverage and enhancing strategic cooperation with our suppliers and customers. Although we expect to continue to increase the volume of imported pharmaceutical products used in our pharmaceutical distribution operations, reflecting the growth of our distribution network and sales in our pharmaceutical

distribution business segment, we intend to maintain our current procurement arrangements and inventory policies with respect to purchasing imported pharmaceutical products from foreign suppliers.

Grow further through acquisitions.

In addition to growing organically, we plan to take advantage of the fragmented nature and rapid growth of the pharmaceutical industry in China to continue to acquire additional pharmaceutical businesses and form partnerships that complement our existing operations, align with our expansion strategies and increase our revenues and profits. We aim to expand and optimize our pharmaceutical distribution operations by capturing merger and acquisition opportunities in order to take advantage of the trend towards consolidation in the PRC pharmaceutical industry. We will select strategic partners and acquisition targets based on a candidate's respective market share, capabilities and reputation in the markets that we seek to enter or where we have not yet established a strong presence. We plan to leverage on the strengths of potential partners and targets to expand our existing market position or establish a presence in a new market. We also believe our past successes in completing and integrating acquisitions, our relationships with many industry participants and our knowledge of, and experience in, the PRC pharmaceutical industry, will attract potential partners and acquisition targets to cooperate with us. Although we currently do not have any specific acquisition plans or targets and have not entered into any definitive agreements with any potential targets, we believe we will be able to identify attractive acquisition targets that complement our existing capabilities and businesses and allow us to continue to grow.

Continue to invest in our efficient logistics and information management systems to improve cost and operating efficiencies.

We intend to continue investing significant resources to upgrade our logistics and information management systems and processes to ensure our competitiveness. As efficient logistics and information management systems are critical to our business and networks, we have invested in advanced logistics systems and taken significant steps to reengineer and integrate our logistics process and reorganize our logistics network. For example, we have utilized distribution order management and warehouse management solution systems in our modern logistics hubs in Beijing, Tianjin, Shanghai, Guangzhou and Shenyang and have integrated those systems with our Enterprise Resource Planning System, or ERP. We also plan to establish regional and provincial logistics facilities equipped with leading technology and information systems. These improvements have provided a direct and high-speed information exchange channel that connects us to our customers and suppliers throughout China, covering each stage of our pharmaceutical distribution operations, including electronic order entry, invoice preparation, purchasing, inventory tracking, GSP-certified warehousing and logistics and delivery arrangements. As a result, we have shortened delivery lead-times, increased responsiveness to customer demands and reduced distribution and selling expenses. We intend to continue to implement new technologies and upgrades in order to obtain additional benefits. In order to capitalize upon the trend to outsource logistics services in the PRC pharmaceutical industry, our subsidiary Sinopharm Logistics is dedicated to logistics arrangements, and will further enhance our logistics service capacities and quality, both for our pharmaceutical distribution operations and third-party logistics customers.

Expand and streamline our total-solution and value-added services.

To enhance the value of our pharmaceutical distribution business, we intend to expand and streamline our value-added services to improve our customers' businesses and reduce their costs. We offer a variety of supplier solutions and advanced logistic services, such as bonded logistics, cold chain warehousing and storage, supply chain consulting, inventory tracking, distribution center management

and technical support and sales assistance to our suppliers and customers. Such a wide range of service offerings not only allows our customers and suppliers to streamline and increase the efficiency of their business by receiving all their desired services in one place, but also further strengthens our relationships with them. We also provide other value-added services, such as electronic purchase order management, quality inspection for imported pharmaceuticals, packaging services, product insurance arrangements, product returns and transportation and delivery services for specialty pharmaceutical products. We will continue to expand our value-added services offerings, as well as to develop our high-end and one-stop shop services, which we believe will enhance our relationships with existing customers and allow us to build relationships with new customers. Further, we will continue to enhance our outsourced third-party logistics services offerings to further diversify our business and create new sources of income. We believe that the continued development of these diversified services will enhance our overall profitability and brand.

Continue to build upon our integrated business platform in order to enhance the synergies between our pharmaceutical distribution, retail pharmacy and other businesses.

We will continue to build upon our integrated business platform in order to enhance the synergies that arise from our pharmaceutical operations spanning the distribution, retail and manufacturing of pharmaceutical and healthcare products and expand our reach to end-customers. We plan to leverage our existing businesses to capitalize on particular opportunities that may arise and create efficiencies and cost savings in our business operations. We also plan to utilize our extensive distribution network to provide reliable supply channels for our retail drug stores which, in turn, will sell the pharmaceutical and healthcare products supplied by our distribution network. Further, we intend to utilize our pharmaceutical manufacturing operations to produce private-label products for our retail pharmacy operations. We expect to maintain the flexibility to reallocate manufacturing capacity of our products in response to potential changes in supply and demand, as well as to control inventory in a way that enables us to meet expected demand for our products.

With operations in multiple segments of the pharmaceutical industry, we are able to maintain control over the quality, supply chain management and marketing of our products. We believe that our integrated business platform maximizes the synergies between our businesses by optimizing our operational efficiency while reducing the costs of our customers, allowing us to further solidify our leadership in the PRC pharmaceutical distribution industry.

OUR BUSINESS SEGMENTS

We are a leading provider of pharmaceutical supply chain services with integrated operations in the following business segments.

- *Pharmaceutical distribution.* This is our principal business. We provide distribution, logistics and other value-added services for pharmaceutical and healthcare products of domestic and international manufacturers and other suppliers.

- *Retail pharmacy.* We have a network of retail drug stores that we directly operate or franchise in major cities throughout China.

- *Other business operations.* In our other business operations, we are engaged in the manufacturing or selling of pharmaceutical products, chemical reagents and laboratory supplies.

The following table sets forth the external segment revenue generated from each of our business segments and the percentage of these revenues to our total revenue for the periods indicated:

	Year ended 31 December						Five months ended 31 May			
	2006		2007		2008		2008		2009	
	(RMB)	(%)	(RMB)	(%)	(RMB)	(%)	(RMB)	(%)	(RMB)	(%)
							(unaudited)			
	(in millions, except for percentages)									
External Segment Revenue:[1][2]										
Pharmaceutical distribution	21,927.2	92.4	28,997.3	93.2	35,745.1	93.6	14,017.7	93.4	16,845.7	93.3
Retail pharmacy	823.1	3.5	835.6	2.7	952.2	2.5	389.0	2.6	463.2	2.6
Other business operations	986.3	4.2	1,277.3	4.1	1,490.2	3.9	600.5	4.0	739.1	4.1
Total external revenue	**23,736.6**	**100.0**	**31,110.2**	**100.0**	**38,187.4**	**100.0**	**15,007.2**	**100.0**	**18,048.0**	**100.0**

(1) External segment revenue refers to segment revenue after inter-segment elimination.

(2) For the years ended 31 December 2006, 2007 and 2008, inter-segment revenues were RMB177.6 million, RMB225.9 million and RMB311.2 million, respectively. For the five months ended 31 May 2008 and 2009, inter-segment revenues were RMB140.9 million and RMB147.6 million, respectively.

PHARMACEUTICAL DISTRIBUTION

Our pharmaceutical distribution operation is our principal business, accounting for more than 90% of our total revenues each year during the Track Record Period. We primarily distribute a full line of prescription and over-the-counter pharmaceutical products, consisting of branded and generic Western and Chinese medicines, as well as healthcare products and medical supplies through a geographically diverse distribution network of 25 distribution centers spanning 19 provinces, municipalities and autonomous regions in China. The ability to control the movement of large volumes of pharmaceutical products, while maintaining product safety and efficacy in a cost-efficient and timely manner, is one of our core competencies. As of 31 May 2009, our direct-sale customers included 4,723 hospitals nationwide, which represented 36.4% of all hospitals in China, encompassing 56.2% of the largest, most highly ranked class-three hospitals. We also distribute prescription and over-the-counter pharmaceutical and healthcare products through our distribution network to other distributors, retail drug stores and other customers, including retail chain stores, independent pharmacies, community clinics and other healthcare institutions. We are one of the only three licensed nationwide anesthetics distributors in China, and we currently hold approximately 90% of the PRC market share of this product. In recent years, we have made intensified efforts to coordinate our nationwide distribution activities by sourcing pharmaceutical products on a centralized basis from domestic and international pharmaceutical manufacturers.

The PRC Central Government has recognized our capability, reliability and efficiency in the distribution of large volumes of pharmaceutical products by including the CNPGC Group, the largest pharmaceutical group in China, in its emergency management and disaster response efforts. Since 1960, the PRC Central Government has allocated to CNPGC central medical reserve funds in order for it to purchase medical products (including medicines) required to respond to major disasters, epidemics and other emergencies. CNPGC is one of the companies designated by the PRC Central Government for management and operation of the central medical reserve funds. Since the principal business of our Company is the distribution of medicines, while that of the other members of the CNPGC Group are other types of businesses, the Controlling Shareholder considers that it is appropriate to re-allocate the funds in relation to medicines to our Company. Please refer to paragraph (1) of the section headed "Relationship with the Controlling Shareholder and the Directors — Independence from the Controlling Shareholder — Financial independence" for further details of the medical reserve funds received by our Company.

BUSINESS

Under a responsibility letter dated 4 January 2006 entered into between CNPGC and the Company, we are responsible for (i) strictly implementing the central medical reserve plan and not changing the types and quantities of medical products purchased and kept without prior permission; (ii) making timely allocations of such medical products in accordance with CNPGC's instructions, which are received from the relevant PRC Government department; (iii) ensuring the quality of such medical products; (iv) ensuring the security of the central medical reserve funds; (v) returning the medical reserve funds to CNPGC unconditionally upon revocation of our duties; (vi) establishing various kinds of rules, policies and measures to manage the central medical reserve funds; and (vii) submitting various kinds of reports to CNPGC in relation to the use of the medical funds and medical products. Other than being responsible for these matters, we do not have any additional costs, benefits, obligations and liabilities after re-allocation and payment of the medical reserve funds to us by CNPGC.

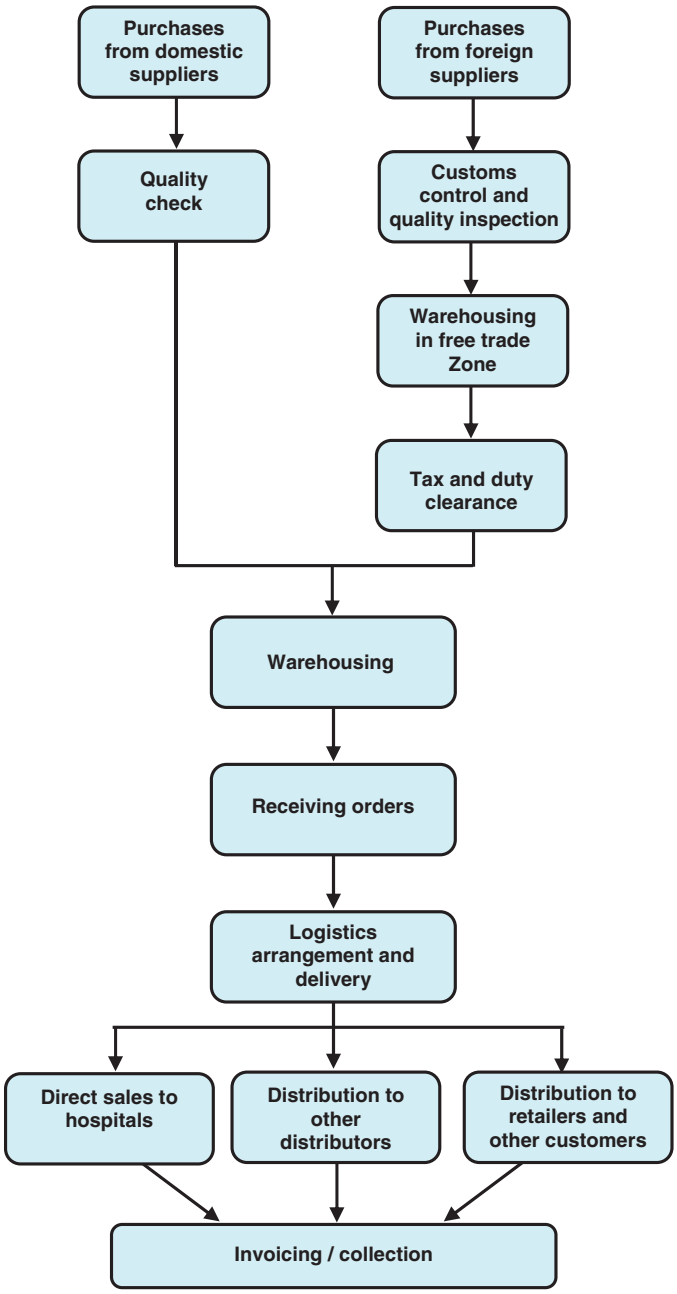
The medical products sold under the responsibility letter to specific customers during major disasters, epidemics and other emergencies were priced at cost. As of 31 December 2006, 2007 and 2008 and 31 May 2008 and 2009, the sale of such medical products by us amounted to nil, RMB507,500, RMB54,970,000, RMB51,615,400 and RMB7,200, respectively.

The following table sets forth a breakdown of the external revenue of our pharmaceutical distribution operations by type of customer during the periods indicated:

	Year ended 31 December						Five months ended 31 May			
	2006		2007		2008		2008		2009	
	(RMB)	(%)	(RMB)	(%)	(RMB)	(%)	(RMB)	(%)	(RMB)	(%)
							(unaudited)			
	(in millions, except for percentages)									
Hospitals	9,642.2	44.0	13,216.6	45.6	16,719.0	46.8	6,563.4	46.8	8,129.7	48.3
Other distributors	10,927.3	49.8	13,753.8	47.4	16,263.6	45.5	6,372.0	45.5	7,134.2	42.3
Retail drug stores and other customers	1,357.7	6.2	2,026.9	7.0	2,762.5	7.7	1,082.3	7.7	1,581.8	9.4
Total	**21,927.2**	**100.0**	**28,997.3**	**100.0**	**35,745.1**	**100.0**	**14,017.7**	**100.0**	**16,845.7**	**100.0**

Operating Process

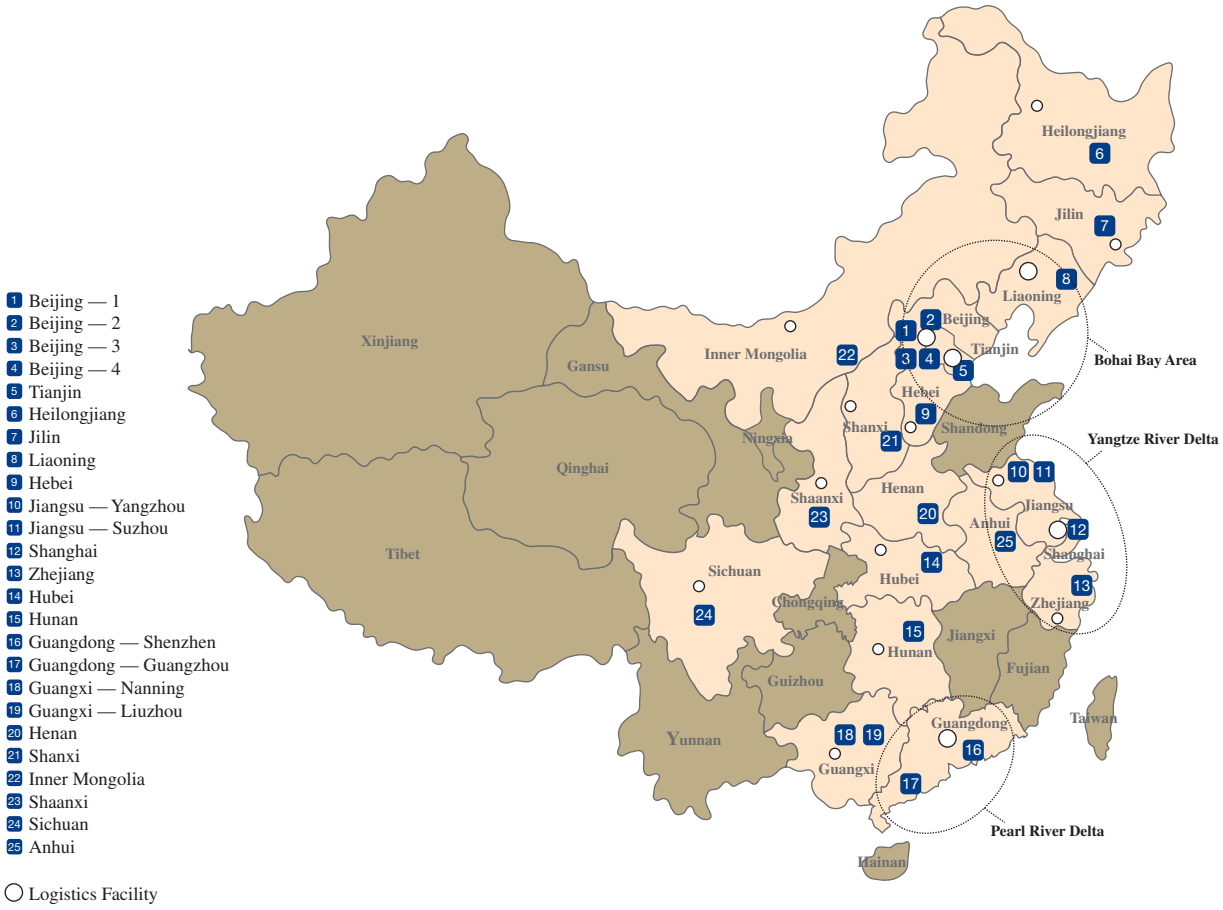
The following diagram illustrates the core operating process of our pharmaceutical distribution operations:



Our pharmaceutical distribution operations involve several integrated procedures that allow for enhanced efficiency and quality control of our products at every stage of our operations, from procurement to delivery to our customers. We purchase products from domestic or foreign suppliers and submit such products through a quality control inspection and assist in clearing any customs and tax matters, if relevant. We warehouse our products in a climate-controlled environment until the receipt of customer orders, during which time we arrange for providing logistics services and the timely delivery of our products. The operating process concludes with the invoicing of, and payment collection from, our customers.

Distribution Network

As of 31 May 2009, we owned and operated 25 distribution centers in 19 provinces, municipalities and autonomous regions across China. The following map illustrates our distribution centers, logistics facilities and the regions directly covered by our sales and marketing teams:



We conduct our pharmaceutical distribution operations through our 25 distribution centers. The primary functions of our distribution centers are to generate sales and manage the daily operations of our operating subsidiaries, such as processing the products received from our suppliers and distributing the products ordered by our customers, as well as storage and warehousing functions. Each distribution center is responsible for sales and marketing activities, such as securing new customers, providing sales and customer support and maintaining existing customer relationships in its operating region. Currently, most distribution centers also serve as coordination centers for the warehousing and transportation logistics of our pharmaceutical distribution operations. We are in the process of centralizing all of our logistics operations in an integrated logistics system under the control of a logistics subsidiary, which we expect to complete in 2010. The distribution centers generally consist of a multifunctional office area, information system, supporting logistics, warehouse facilities and receiving and shipping docks. Our distribution centers generally range in size from 5,000 sq.m to 20,000 sq.m of gross floor area and our warehouses range in size from 3,000 sq.m to 20,000 sq.m of gross floor area.

Sales and Marketing

We make our pharmaceutical distribution sales primarily in China. The following table sets forth a geographical breakdown of the revenue, after inter-segment elimination, from our pharmaceutical distribution operations for the periods indicated:

	Year ended 31 December						Five months ended 31 May			
	2006		2007		2008		2008		2009	
	(RMB)	(%)	(RMB)	(%)	(RMB)	(%)	(RMB)	(%)	(RMB)	(%)
	(in millions, except for percentages)									
Bohai Bay	8,373.9	38.2	12,707.9	43.8	15,214.6	42.6	6,043.9	43.1	7,291.9	43.2
Yangtze River Delta	5,888.6	26.9	6,896.8	23.8	8,754.1	24.5	3,513.9	25.1	3,743.3	22.2
Pearl River Delta	5,324.8	24.3	6,196.3	21.4	8,117.0	22.7	3,138.7	22.4	3,764.8	22.4
Other regions	2,339.9	10.6	3,196.4	11.0	3,659.4	10.2	1,321.3	9.4	2,045.7	12.1
Total	**21,927.2**	**100.0**	**28,997.3**	**100.0**	**35,745.1**	**100.0**	**14,017.7**	**100.0**	**16,845.7**	**100.0**

As of 31 May 2009, our direct customers included 4,723 hospitals, including 670 class-three hospitals, 2,545 distributors, over 22,000 retail pharmacies and other customers. The following table sets forth below a geographical breakdown of our customers:

	Hospitals	Distributor customers	Retail pharmacies and other customers
Bohai Bay	1,218	388	7,652
Yangtze River Delta	782	313	3,961
Pearl River Delta	880	557	6,191
Other Regions	1,843	1,287	4,351
Total	**4,723**	**2,545**	**22,155**

As of 31 May 2009, we had approximately 1,651 sales and marketing representatives for our pharmaceutical distribution operations, who were located at our head office as well as in our regional distribution centers.

Our 256 sales and marketing representatives located at our head office are primarily responsible for the sales and marketing activities of the daily distribution operations of the Company as well as developing general marketing and promotional plans for our pharmaceutical distribution business on a company-wide basis. The corporate sales and marketing department at our head office also designs and develops service packages to provide value-added services. These service packages are tailored to specific customer groups and can be further customized at the distribution facility level to adapt to local market conditions. Further, our corporate sales and marketing department at our head office serve national account customers in close cooperation with our local distribution centers. Each of our distribution centers is electronically linked to our central computer system and information management network, thus facilitating our control over purchasing, shipping and billing.

Our 1,395 sales and marketing representatives located at our distribution centers are primarily responsible for undertaking regional sales, marketing and customer support activities directly to customers. Because our sales and marketing representatives are located in our distribution centers, which are strategically located close to customers in each of the regions where we do business, they are able to respond promptly to customer needs in an effective manner. Our sales and marketing representatives at our distribution centers carry out the marketing and promotional plans developed at our head office, and conduct a review process to screen customers before engaging in sales and marketing efforts.

Our sales personnel in our sales and distribution centers are organized by the geographical coverage of our distribution network and are further specialized by particular type of customer, sale method and product category. We mainly provide pharmaceutical distribution services through: (i) a direct sales force that primarily sells prescription medicines to national and regional hospitals; (ii) a sales force that primarily sells pharmaceutical and healthcare products to other distributors; (iii) a general sales force that primarily sells pharmaceutical and healthcare products to retail drug stores and other end-customers; and (iv) sales teams that specialize in the distribution of anesthetics and vaccines.

Manufacturers generally sell their products exclusively to pharmaceutical distributors, such as ourselves, which in turn sell their products to hospitals, other distributors, retail pharmacies and other customers. We believe they do so because it is a cost-effective way to reach a broad end-user base.

Sales and Distribution Agreements

The majority of our product sales are based on recurring customer purchase orders. Generally, we do not enter into any long-term contracts. In addition, we utilize different sales and distribution agreements for different types of customers.

Hospital customers

Our direct sales to public hospitals are primarily channeled through the PRC Government-mandated collective hospital tendering process, through which a hospital solicits public bids from pharmaceutical manufacturers as part of its pharmaceutical procurement process. See the section headed "Regulation — Tendering Requirements for Hospital Purchases of Medicines" in this document. The tendering process generally takes three to six months to complete. The collective bidding process covers multiple categories of medicines used by public hospitals and, although the number varies by geographic region, approximately thousands of pharmaceutical manufacturers generally participate in the collective hospital tendering process. The supply of a particular type of medicine is generally made on a non-exclusive basis by multiple manufacturers and distributors. We enter into distribution agreements with the manufacturers and advise them in the collective hospital bidding process. We work closely with the manufacturers to improve their bidding position and number of successful bids by providing industry expertise, market intelligence, competitive price suggestions, documentation support and other administrative services. We typically advise and assist multiple manufacturers in the same hospital tendering process, including our own pharmaceutical manufacturing subsidiaries. The duly organized bidding evaluation committee of pharmaceutical and clinical medical experts determines which manufacturers win bids and hospitals determine the dosage form, manufacturer and brand of a particular drug delivered through placing purchase orders with us after the bidding process. After the tendering process, we distribute products of the pharmaceutical manufacturers that win bids upon purchase orders provided by the hospital, which will specify the brand, volume and types of pharmaceutical products. The pricing of these products will be determined in accordance with the collective hospital bidding process. As a result, during the Track Record Period, we did not experience any material conflicts from advising both our subsidiaries as well as other independent third-party pharmaceutical manufacturers in the same tendering process.

Distributor customers

We sell our products to distributor customers because we currently do not directly cover every province or autonomous region in China and some distributors have sale channels to reach hospitals, retail pharmacies and other healthcare institutions that are not in our customer base.

Our distribution and sales of pharmaceutical products to distributor customers are generally governed by three-party negotiations among pharmaceutical manufacturers, us and the downstream

distributors. From time to time, pharmaceutical manufacturers will enter into written three-party agreements with us and our distributor customers. However, under prevailing industry practice in the PRC, entry into a written three-party agreement is optional, and the parties will not necessarily enter into a written three-party agreement. The three-party agreements generally specify the suggested selling price of pharmaceutical products, which is ultimately subject to price ceilings or other forms of price controls set by the PRC Government, upon their subsequent sale and distribution by the distributor customer, the qualifications of the distributor customer and the exclusivity, term period and geographic coverage of the distribution and sales of such products by our distributor customers, as well as order, delivery and payment arrangements between us and the distributor customers. Pharmaceutical manufacturers will generally specify different suggested selling prices for hospitals and retail pharmacies in the three-party agreements. Our selling price of the pharmaceutical products to the pharmaceutical distributor customers is governed by distribution and agency agreements entered into separately between us and the pharmaceutical manufacturers. Downstream distributors order products from us and we are responsible for the supply and delivery of such products. In certain three-party agreements, our distributor customers are required to submit monthly sales and inventory reports to the pharmaceutical manufacturers for review. The terms of the three-party agreements range from one year to three years. However, the majority are for a term of one year and are renewable for one year or more upon their expiration.

Except for 36 distributor customers which are our connected persons, our distributor customers are independent third parties. Sales of pharmaceutical products, healthcare products and medical supplies to these 36 distributor customers for the years ended 31 December 2006, 2007, 2008 and the five months ended 31 May 2009 were approximately RMB674 million, RMB751 million, RMB902 million and RMB323 million, respectively, representing approximately 3.1%, 2.6%, 2.5% and 1.9% of our total revenue in our pharmaceutical distribution segment.

We select our distributor customers based on a variety of criteria, such as their credit record, customer portfolio and distribution network. The following table sets forth the changes in the number of our distributor customers during the Track Record Period:

	Year ended 31 December			Five months ended 31 May
	2006	2007	2008	2009
Additions of new customers	327	148	102	267
Termination of existing customers	(391)	(703)	(758)	(725)
Net decrease in distributor customers	(64)	(555)	(656)	(458)
At the end of year/period	4,214	3,659	3,003	2,545

The decrease in the number of our distributor customers during the Track Record Period was primarily due to our stricter standards to select and maintain distributor customers and the expansion of our own direct geographical coverage of pharmaceutical customers. The decrease was also consistent with the trend towards consolidation in the pharmaceutical distribution industry in China.

Other customers

In addition, we have direct sales to retail drug stores and other customers such as retail chain stores, independent pharmacies, community clinics and other healthcare institutions. The majority of our product sales to these customers are based on recurring customer purchase orders.

Revenue recognition and pricing

We recognize revenue from the sales of goods to our customers when our products are delivered to the hospital, retail pharmacy or distributor customer, the customer has full discretion over the channel and price to sell the products, and there is no unfulfilled obligation that could affect the

customer's acceptance of the products. As our products are often sold with volume discounts, sales are recorded based on the price specified in the sales contracts, net of the estimated volume discounts at the time of sale.

In principle and customary with market practice, the price of our products is determined through the PRC Government-mandated collective tender process and/or negotiations with our suppliers and customers. Negotiations take into account various factors, including our procurement costs and gross margin levels, our extensive distribution network and bargaining power, government policies and regulations, competition, customer preferences and market considerations.

Payment

Our customers are generally invoiced at the time of delivery of their order, with varying credit terms, generally ranging from 30 to 120 days. Our extension of credit terms depends, in part, on the creditworthiness of certain customers, the location of customers and the products being sold. We accept payments from our customers in the form of bank note, wire transfer or cash.

Sales returns

For sales returns, our customers may return products that are damaged, with incomplete packages, unclear labels or missing contents or inconsistent with the specifications on the purchase orders. In addition, our customers may return the products which cease to be on public hospitals' pharmaceutical procurement lists or have expired or are close-to-expiry. For certain pharmaceutical products, we are required to obtain pharmaceutical manufacturers' prior approval before accepting sales returns from our customers. For products that are not damaged, that are complete, that are consistent with the specifications on the purchase orders and that expire more than six months following the date of the requested sales return, we only accept the sales return if the products may be resold or returned to the supplier for full credit. During the Track Record Period, our monthly sales to our customers, including downstream distributors, were generally stable and we did not have a material amount of sale returns from our customers. Our sales returns were approximately RMB362.2 million, RMB468.4 million, RMB615.0 million and RMB271.2 million for the years ended 31 December 2006, 2007 and 2008 and the five months ended 31 May 2009, respectively.

Product Portfolio

We leverage our extensive pharmaceutical expertise and capitalize on our close relationships with key suppliers to offer quality products and services to our customers. As of the Latest Practicable Date, we distributed 46 of the 50 international top-selling pharmaceutical products in China. As of 31 May 2009, we distributed over 22,000 different types of pharmaceutical and healthcare products, including prescription medicines, consisting of branded and generic medicines, and over-the-counter medicines as well as personal care products and medical supplies. During the Track Record Period, our sales of personal care and medical supplies products accounted for less than 0.2% of our total revenue generated from pharmaceutical distribution operations. Our products are provided by over 3,300 suppliers, comprising both international and domestic pharmaceutical companies. Our suppliers include 30 of the top 50 international pharmaceutical companies, such as Roche, AstraZeneca, Pfizer, GlaxoSmithKline, Novo Nordisk, Merck and Eli Lilly, and 95 of the top 100 domestic pharmaceutical companies, such as Jiangsu Hengrui, Harbin Pharma and North China Pharma. In addition, we are also one of the only three licensed nationwide anesthetic distributors in China, and we currently hold approximately 90% of the PRC market share for anesthetics.

As of 31 May 2009, we managed the storage and transportation of approximately 17,600 prescription medicines and approximately 4,300 over-the-counter medicines in our pharmaceutical distribution operations. We distribute these prescription and over-the-counter medicines to hospitals,

other distributors, retail pharmacies, community clinics and other healthcare institutions. We believe we are currently the only distributor in China appointed by the relevant suppliers with respect to 162 of our pharmaceutical products, although, consistent with market practice for suppliers in China, our distribution agreements with these suppliers are not stated to be on an exclusive basis. The table below sets forth the major treatment areas of our prescription and over-the-counter pharmaceutical products, the number of products for each treatment area and the major products in each category:

Product category	Number of products[1]	Major products
Medicines for digestive and metabolic diseases	4,400	Ademetionine for injection, Gemcitabine Hydrochloride for injection, Montmorillonite powder, Domperidone tablet, Esomeprazole Magnesium enteric-coated tablet, Omeprazole Sodium for injection, Hydrotalcite tablet, Ademetionine Enteric-coated tablet, Ursodeoxycholic Acid capsule
Medicines for cardiovascular diseases	3,300	Atorvastatin Calcium tablet, Felodipine sustained release tablet, Telmisartan tablet, Levamlodipine Besylatetablet, Valsartan capsule, Metoprolol Tartrate sustained release tablet, Nifedipine controlled-release tablet, Metoprolol Tartrate sustained release tablet, Metoprolol Tartrate tablet and Lossartan Potassium tablet
Anti-infection medicines	3,200	Imipenemand Cilastatin Sodium for injection, Meropenem for injection, Cefaxolin Sodium for injection, Vancomycin Hydrochloride for injection, Ceftazidime for injection, Teicoplanin for injection, Ceftriaxone sodium for injection, Cefoperazone Sodium/Sulbactam Sodium for injection, Meropenem for injection and Cefaclor for suspension
Medicines for cancer and immune system diseases	600	Mycophenolate Moretil capsule, Gefitinib tablet, Capecitabinen tablet, Gemcitabine Hydrochloride for injection, Paclitaxel injection, Letrozole tablet, Rituximab injection, Pemetrexed disodium for injection, and Mycophenolate Moretil capsule
Medicines for psychiatric diseases	1,100	Olanzapine tablet, Fluoxetine Hydrochloride dispersible tablet, Proxetine Hydrochloride tablet, Levodopa and Benserazide tablet, Risperidone tablet, Sertraline Hydrochloride tablet, Sodium Valproate sustained release tablet, Oxiracetam injection, Bromocriptine Mesilate tablet and Almitrine Bismesylate/Raubasine tablet
Medicines for respiratory system	2,000	Ambroxol Hydrochloride injection, Ambroxol Hydrochloride tablet, Ambroxol Hydrochloride oral solution, Myrtol Standardized enteric-coated soft capsule, Ipratropium Bromide solution for inhalation, Compound Codeine Phosphate solution, Compound Ipratropium Bromide solution for inhalation, Salmeterol Xinafoate and Fluticasone Propionate powder for inhalation
Medicines for blood and hemoglobin producing system	500	Clopidogrel Hydrogensulfate tablet, Octreotide Acetate injection, Mecobalamin tablet, Mecobalamin injection, Hydroxyethyl Starch 130/0.4 and Sodium Chloride injection, Cobamamide for injection and Alteplase for injection Succinylated Gelatin injection
Medicines for muscular and skeleton system	700	Glucosamine Hydrochloride capsule, Calcium Carbonate and Vitamin D3 tablet, Compound Calcium Gluconate oral solution, Meloxicam tablet, Calcitriol Soft capsule, Alendronate Sodium tablet, Diclofenac Sodium enteric-coated tablet and Calcitriol soft capsule

(1) Figures provided are approximate figures.

Product category	Number of products[1]	Major products
Hormone preparation (excluding sex hormome)	300	Isophane Protamine Biosynthetic Human Insulin injection (Pre-mixed 30R), Repaglinide tablet, Gliclazide tablet (II), Repaglinide tablet, Acarbose tablet, Isophane Protamine, Biosynthetic Human Insulin injection (Pre-mixed 50R), Salcatonin injection, Gliclazide preparation powder, Mixed Protamine Zinc Recombinant Human Insulin injection and Biosynthetic HumanInsulin injection
Dermatology Medicines	1,000	Miconazole Nitrate cream, Mupirocin cream, Triamcinolone Acetonide and Econazole cream, Halometasone/Triclosan cream, Mometasone Furoate cream Halometasone cream, Minocycline Hydrochloride ointment, Compound, Dexamethasone Acetate cream, Halometasone cream, Ketoconazole
Medicines for sensing system	900	Verteporfin for injection, Weianlin eye drop, Sodium Hyaluronate eye drop, Sodium Hyaluronate injection, Iodized Lecithin tablet, Ofloxacin eye drop, Levofloxacin Hydrochloride eye drop, Pirenoxine eye drop, Vitamin A palmitate gel and Compound Chondroitin Sulfate eye drop
Medicines for reproductive and urinary system and sex hormone	700	Finasteride tablet, Alprostadil injection, Goserelin Acetate sustained release depot, Epristeride tablet, Prostat tablet, Ethinylestradiol and Cyproterone Acetate tablet, Desogestrel and Ethinylestradiol tablet, Valerate tablet, Conjugated Estrogens tablet, Dydrogesterone tablet
Parasiticide, insecticide and insect repellent	200	Abendazole tablet, Ornidazole injection, Ornidazole and Sodium Chloride injection, Ornidazole for injection, Hydroxychloroquine Sulfate tablet, and Ornidazole capsule
API and medicines not for direct intake	30	Iodine, Sirolimus oral solution, Basiliximab for injection, Sirolimus tablet, Misoprostol HPMC and Sirolimus oral solution
Miscellaneous	100	Peginterferon alfa-2a solution for injection, Peginterferon alfa-2a solution for injection Trastuzumab injection, Sevoflurane, Propofol injection, Iopromide injection, Propofol injection, Iopromide injection and Recombinant Coagulation Factor VIII for injection

(1) Figures provided are approximate figures.

The following table sets forth our personal care and medical supplies products, the number of products and the major products in each category:

Product category	Number of products[1]	Major products
Personal care products	700	Throat lozenges, Liquid dosage supplements, Health supplements and Dietary supplements
Medical supplies products	600	Syringes, Needles, Blood sugar testing paper and Compressors

(1) Figures provided are approximate figures.

Value-added Services

We provide value-added supply chain services, such as supplier solutions, certain advanced logistics and other value-added services. For example, we utilize packaging, processing, storage and transportation methods designed especially for specialty medicines that are valuable, fragile, perishable

or require specific handling methods. The depth and breadth of our services reduce our customers' inventory and fulfillment costs and other operational expenses. In addition, we are able to provide our suppliers with valuable market data and information that we collect during the course of our operations with our information management system, as well as certain advanced services of inventory tracking and management, distribution center management and supply chain management consulting. Our value-added services benefit our customers by allowing them to efficiently deliver healthcare products, while lowering their overall costs that are associated with the pharmaceutical supply chain. In addition, our value-added services benefit our suppliers by setting strict quality control measures and ensuring the timely distribution of their products. We generally do not charge our customers or suppliers separate fees for our value-added services, and thus do not receive material revenues from these services; however, we have a long-term plan to generate additional revenues in the future from value-added services as part of our existing pharmaceutical distribution operations. These services have also strengthened our existing supplier and customer relationships, differentiated us from our competitors and enabled us to pursue new relationships with key healthcare product suppliers.

The following table sets forth our value-added services, supply-side solutions and advanced logistics services:

Category	Services
Supplier solutions	Import agency Customs clearance Free trade zone warehousing Pharmaceutical inventory management Collection services on behalf of the suppliers
Advanced logistics services	Inventory analysis report Design and establishment of supply chain Technical support and sales assistance Inventory tracking and management
Other value-added services	Electronic purchase orders and confirmation Quality inspection for imported pharmaceuticals Packaging, repackaging and reprocessing services Product insurance arrangement Product return or replacement Delivery of specialty pharmaceutical products

Supplier Arrangements

We categorize our suppliers into different levels for the purpose of supplier management, such as strategic alliance suppliers, agreement suppliers and suppliers on a transaction-to-transaction basis. We maintain relationships with our strategic alliance suppliers by entering into annual agency or distribution agreements. Under these agreements, we enhance the product promotion of such suppliers, provide feedback on sales of their products and maintain close communications with these suppliers. Our agreement suppliers are characterized as parties with whom we have had multiple agreements or repeat transactions with, but with whom we do not cooperate at the same level as we do with our strategic alliance suppliers. Our transaction-to-transaction suppliers are generally newer, less familiar suppliers that have smaller agreements with us in terms of volume.

The cost of purchasing merchandise paid to our suppliers is generally determined through negotiation, which generally involves our suppliers and customers, during the procurement process. Currently, the procurement of our products is mainly conducted by our subsidiaries with the assistance and guidance of our head office, and partially through centralized procurement coordinated by our head office. In order to enhance our economies of scale, we have begun to implement measures to

coordinate our nationwide distribution activities by sourcing pharmaceutical products on a consolidated basis and to centralize procurement from our regional subsidiaries to our national head office. We believe that a centralized procurement policy will enable us to exercise more bargaining power with respect to price and other contract terms, strengthen our negotiating position with our suppliers and integrate our logistics services. An integrated purchasing network will also make us more attractive to our customers and enhance the competitiveness of our pharmaceutical distribution operations.

We have had business relationships with most of our suppliers since the incorporation of the Company in 2003. The terms of the agreements we enter into with our suppliers for pharmaceutical distribution operations range from one year to three years. However, most are for a term of one year and are renewable for one year or more upon their expiration. During the Track Record Period, we did not experience any difficulty in renewing our agreements with suppliers.

These agreements set out the specifications and prices for the suppliers' pharmaceutical products, credit periods, guidelines for the sale and distribution of their products, including restrictions on the regions in which the products may be sold, as well as the terms of any logistics services that may be provided. Under the agreements, the suppliers are responsible for ensuring the quality of, and the validity of its intellectual property rights to, their pharmaceutical products. We are responsible for timely delivery of products and payments to the suppliers as well as compliance with guidelines set by our suppliers, especially the suggested selling price. Suppliers also typically prescribe a minimum or target purchase amount, and may engage our assistance in the hospital tendering process and in their sales and promotion activities. In general, the suppliers will not terminate the agreements if we fail to meet such target purchase amount. The agreement may be renewed or extended upon mutual agreement in writing before its expiration date. The suppliers may terminate the agreements if we breach major contract terms, such as if we fail to comply with the guidelines of the distributor specified in the agreements, or if we delay the product delivery to our customers or if we are delinquent in making payment.

The credit terms granted by our suppliers are generally up to 180 days. We settle outstanding payables with our suppliers through bank note and wire transfer. Certain suppliers will provide us rebates for early payments.

For purchase returns, we are able to return products that are damaged, have incomplete packages/unclear labels or are missing contents, have expired, are close-to-expiry or do not otherwise satisfy our quality standards by notifying the supplier during the specified return period. To a lesser extent, we may return certain pharmaceutical products back to suppliers if such products cease to be on public hospitals' pharmaceutical procurement lists. During the Track Record Period, we did not have a material amount of returns of purchases to our suppliers.

Logistics Arrangements and Infrastructure

As a part of our pharmaceutical distribution operations, we provide comprehensive and technologically-advanced logistics arrangements to our suppliers and customers which cover the entire range of the pharmaceutical supply chain in China. We generally do not charge separate fees for our logistics arrangements and facilities. Our logistics services help our customers improve their service quality and reduce costs, meet evolving demands in less time, synchronize their logistics with end-customers' demands, improve process efficiency and enhance supply chain visibility. Our pharmaceutical logistics arrangements mainly consist of storage, warehousing, and long-distance, regional and local transportation and delivery services. We are also a leading provider of outsourced logistics services to the pharmaceutical and healthcare industry. Our healthcare capability is integrated

with national freight management, enabling our third-party customers to benefit from end-to-end supply chain management through a single point of contact. As a testament to our capabilities and services, we are the main national provider of outsourced logistics services for GlaxoSmithKline and Bayer. Other outsourced logistics services customers include domestic and international pharmaceutical companies such as Bausch & Lomb Incorporated, Eli Lilly, and Kangmei Pharmaceutical Co., Ltd.

Our demand-driven logistics arrangements aim to manage the flow of products and information with high efficiency and precision, as well as minimize our inventory holding costs. We typically deliver our products to our customers on a daily basis. Our integrated services are custom-designed to meet the unique requirements of the pharmaceutical and healthcare industry, and our operations have the stringent procedural controls and monitoring required in a regulated business environment. Our warehouses are equipped with comprehensive Warehouse Management Systems, or WMS, including automatic systems for the selection and transportation of goods, as well as climate control. We also use tracking systems employing radio-frequency identification, or RFID, which is an automatic product identification system that utilizes small transponders and radio signals to quickly retrieve product data and location in logistics facilities. We have further reduced the delivery lead-time in our logistics facilities by introducing a night shift to repackage and assemble orders. In general, orders generally leave our warehouses within six hours of our receipt of customer orders. During the Track Record Period, we did not encounter any material errors or delays in our logistic arrangements for our pharmaceutical distribution operations.

Our regional and local logistics facilities located at our distribution centers are primarily responsible for the coordination and provision of integrated regional logistics services. They generally consist of storage space and related logistics equipment and range in size from 5,000 sq.m to 20,000 sq.m in terms of gross floor area. We commenced an upgrade and integration plan for the infrastructure of our logistics facilities in 2007 with the aim to establish a fully centralized logistics system in 2010. Each facility is organized according to the volume of products distributed by, and total floor space of, the facility. This reflects whether the service area of the facility is regional, provincial or local. Our five integrated regional logistics hubs are located in Beijing, Tianjin, Shanghai, Guangzhou and Shenyang. These hubs directly serve our customers and act as coordination and planning centers for other logistics facilities. We are in the process of upgrading certain existing facilities to become integrated provincial facilities. They are located in the provinces or autonomous regions of Zhejiang, Jiangsu, Hubei, Hunan, Shanxi, Shaanxi, Henan, Sichuan, Guangdong, Liaoning, Jilin, Heilongjiang, Inner Mongolia and Guangxi. We also intend to establish smaller local facilities in other selected cities across China to further extend our reach to end-customers. We believe this system will increase our scale of operations, broaden our geographical coverage and better serve our customers and suppliers.

Information System

Our logistics and information management system provides for, among other things, electronic order entry by customers, invoice preparation and purchasing and inventory tracking. The efficient distribution of small orders is possible through the extensive use of computerization and modern warehousing techniques, which include computerized and automated warehouse product location, bar-coding systems, routing and inventory notification and replenishment systems, gravity-flow racking, mechanized order selection and efficient truck loading and routing. We integrate various systems such as WMS, Chain Management System, or CMS, Hospital Information System, or HIS, and a centralized inventory system managing warehouses across different locations to establish a standardized platform for electronic business management which is used by various suppliers and hospitals. We also integrate distributed order management and warehouse management solution systems, which is utilized with our ERP system, providing a platform for a number of basic and value-

added services provided to our customers, including marketing, product demand data, inventory replenishment, computer price updates and price labels, in turn realizing a direct and high-speed information exchange channel connecting us to our customers. Each of these functions enables us to exercise more precise control over our inventory flow, enhance our logistics and value-added services offerings, improve our operational planning and strengthen our customer relationships.

We are committed to the continuing development of our integrated information system. We have established four warehouses in Beijing, Shanghai Tianjin and Guangzhou that are equipped with modern logistics information systems. We use the WMS, a comprehensive and powerful inventory management system with enhanced inventory tracking and analysis, in our regional and provincial logistics centers. Each of our logistics centers can process 100,000 purchase orders daily. Our developing information platform mainly consists of an integrated national platform, regional purchase order processing systems, inventory management systems and pricing management systems. Our information system is connected through CMS to the management systems of our end-customers, including the logistics centers of such end-customers. This integrated management system allows for expansive coverage of our information network as well as the sharing of information and resources. Our information system is utilized by domestic and international suppliers such as GlaxoSmithKline and Dainippon Sumitomo Pharmaceutical Co., Ltd. We aim to optimize the profitability of our operations by maintaining inventory specific to the requirements of the local market served by each facility.

Furthermore, in order to prevent any disruption of our information system as well as to respond to unforeseeable events or system failures and timely resume system operations, we have developed a disaster recovery plan for our information system. Upon the failure or disruption of our intranet, we may access a backup virtual private network system through the internet. We have also implemented a standby mechanism, through which we maintain primary and secondary information systems. All data is mirrored to the secondary server in real time so that both systems contain identical information. In this way, we are able to switch to the secondary system upon the failure or disruption of the primary system. During the Track Record Period, we did not encounter any significant system failures or disruptions to our information system.

RETAIL PHARMACY

We are one of the leading retail pharmacy operators in the PRC retail pharmacy market. According to China Pharmacy Magazine, we were among the top five pharmaceutical retailers in China, in terms of the number of retail stores in the year ended 31 December 2008. We have developed a number of retail pharmacy brand names such as 大德生 (Dadesheng) and 一致 (Accord) in many major cities in China. As of 31 May 2009, we directly operated 632 retail pharmacies and had 186 franchise retail pharmacies in premium locations situated in seven of the largest and most developed provinces and municipalities, including Zhejiang, Beijing, Shanghai, Tianjin, Jiangsu, Liaoning and Guangdong, as well as in two autonomous regions.

BUSINESS

Retail Network

We believe we have succeeded in building a retail pharmacy chain with an extensive geographical reach throughout China. The following table sets forth the number of our self-operated and franchise retail drug stores by city or province as of the dates indicated:

	As of 31 December									As of 31 May		
	2006			2007			2008			2009		
City or Province	Directly owned	Franchise	Total	Directly owned	Franchise	Total	Directly owned	Franchise	Total	Directly owned	Franchise	Total
Guangdong Province	187	89	276	184	88	272	170	76	246	196	78	274
Shanghai	53	112	165	68	115	183	76	56	132	81	58	139
Jiangsu Province	86	14	100	87	14	101	83	7	90	80	8	88
Beijing	44	0	44	51	0	51	37	0	37	41	0	41
Liaoning Province	5	0	5	6	0	6	30	33	63	43	34	77
Others	50	2	52	50	2	52	72	7	79	191	8	199
Total	**425**	**217**	**642**	**446**	**219**	**665**	**468**	**179**	**647**	**632**	**186**	**818**

The following table set forth the changes in the number of our retail drug stores during the Track Record Period:

	Year ended 31 December			Five months ended 31 May
	2006	2007	2008	2009
At the commencement of year/period	548	642	665	647
Additions of new retail drug stores	136	58	36	185
Termination of existing retail drug stores	(42)	(35)	(54)	(14)
Net increase in retail drug stores	94	23	82	71
At the end of year/period	642	665	647	818

The continued growth and success of our retail business will depend on the results of our expansion plan to add new pharmacy stores. Our expansion plan focuses on both entering new markets and adding stores within existing markets. We plan to focus on developing directly owned pharmacy stores. We also plan to add specialty stores that focus on high-end consumer health and cosmetic products to our retail network, and to a lesser extent, other retail operations such as discount stores. During the Track Record Period, the number of our directly owned stores increased, primarily due to the openings of our new directly owned stores and acquisitions of the retail pharmacy stores of Shenyang Tianyitang and Zhejiang Intmedic in 2008 and the State-owned Assets Supervision and Administrative Commission of the Ningxia Autonomous Region in 2009. This increase was partially offset by the closing of some directly owned stores following our review of the performance of our stores and in conjunction with PRC Government urban renewal and relocation policies. During the Track Record Period, the number of our franchise stores decreased, primarily due to (i) the expiration in November 2008 of our franchise agreement with Shanghai Shanghong Pharmacy Chain Store Co., Ltd., which operated 59 retail pharmacies in Shanghai, and (ii) the enhanced monitoring and management of our franchise stores with respect to their service quality and compliance with the terms of the franchise agreement. Because of these stricter monitoring and management measures, we disqualified certain franchise stores for their failure to comply with the terms specified in the franchise agreement or to meet our standards for operation and service and some franchise stores also voluntarily terminated their franchise arrangements with us.

We believe that increasing our store base in, and relocating stores to, desirable geographical markets are essential strategies for competing effectively in the current environment and maintaining our leading position in the retail pharmacy market.

Directly owned stores

As of 31 May 2009, we had approximately 632 directly owned stores. We carefully select our store sites to maximize consumer traffic, store visibility and convenience for our customers. Substantially all of our stores are located in well-developed urban residential communities and prime retail locations in seven provinces and municipalities in China.

Franchises

As of 31 May 2009, we had 186 franchise stores primarily located in the city of Shanghai and Jiangsu, Guangdong, Liaoning, Guangxi and Zhejiang provinces. We identify and select independent local stores that maintain certain levels of sales volumes and are positioned in favorable locations to serve as our franchises. Franchise stores operate under our retail brands, and we receive a franchise fee that is calculated on the basis of the total revenue of such store as well as a fee for being the preferred supplier of products and logistics services for the franchise store. For the years ended 31 December 2006, 2007 and 2008 and the five months ended 31 May 2009, our franchise fees amounted to RMB11.6 million, RMB10.9 million, RMB15.3 million and RMB3.9 million, respectively. Through franchising, we are also able to increase our brand awareness among retail end-customers. To maintain our quality standards and brand reputation, we inspect our franchise stores on a regular basis.

Under the terms of our franchise agreements, we require our franchisees to fulfill a number of obligations, including: (i) operating under our retail pharmacy brand; (ii) sourcing all the products they carry from us; (iii) maintaining all necessary permits and licenses for operations and store facilities; (iv) recruiting qualified professionals and employees; (v) implementing our pricing policies; and (vi) maintaining our uniform store design and layout. However, in the franchise agreement, we do not prescribe any minimum purchase amount for our franchise stores to source products from us. Our franchise agreements generally have a termination date of five years from the date of the agreement, subject to renewal or extension of the franchise arrangement upon mutual agreement of the parties.

Pursuant to the franchise agreements, we provide various services for our franchisees to ensure the sale of our products, including management and employee training programs and advertising, marketing and promotional services. The franchise stores may return products before their expiration dates if such products are found damaged or incomplete, and may also return products that have expired. As our franchise stores must source all their products from us, we are fully responsible and liable for the products provided by us and sold through our franchise stores.

Store operations

We have developed a uniform and distinct layout, color scheme and design specifications, which promotes the corporate image of our retail drug stores. Our stores are staffed with an in-store pharmacist, who primarily consults with customers and assists with the dispensing of prescription drugs. In addition, we regularly carry out training programs on medicine information, nutritional information and selling skills and customer interaction for our store staff and pharmacists, as well as management training for our regional and senior managers and management officers.

Although we offer our retail customers the option to pay by cash or debit or credit cards, or by medical insurance cards, the substantial portion of retail sales are made in cash. As such, we have

adopted strict cash control procedures in all of our retail drug stores. In particular, the details of each sale are recorded in our integrated information management system, and the cash generated from our stores is deposited in a controlled, on-premises safety-deposit box in each of our retail stores. Our finance department undertakes a daily reconciliation of sales data collected from cash deposit receipts that is subsequently confirmed by our banks.

We recognize revenue from the sale of goods to our retail customer in our directly owned stores when the products are sold to the customer. We recognize revenue from the sale of goods to our franchise stores when our products are delivered to the franchise stores. We recognize revenue from the fees paid by our franchise stores when all material services relating to the franchise agreement have been substantially performed.

We obtain reimbursements every one to three months from the relevant government social security bureaus for sales made to eligible participants in the national medical insurance program, depending on the province in which a store is located. Such reimbursements are the primary account receivables for our retail drug stores, as we generally do not grant credit to our retail customers. As of 31 May 2009, 361, or 44.1% of our stores, were designated stores under the PRC national medical insurance program.

Products and Services

We provide our customers with convenient and professional pharmacy services and a wide variety of healthcare products. Our typical retail drug store sells prescription medicines and a wide assortment of general healthcare products that are nationally advertised brands or our private-label products. Front store categories include many of the world's well-known over-the-counter medicines, including medication for skin care, eye care, oral care, upper respiratory, gastrointestinal, hair growth and tobacco dependence as well as beauty products and cosmetics.

Product offerings

Our merchandise can be broadly classified into the following categories:

Prescription medicines. We offer a wide variety of medicines that comprise 19 of the 23 currently available classes of prescription medicines. We accept prescriptions only from physicians and other licensed healthcare service providers. Our in-store pharmacists verify the validity, accuracy and completeness of all prescription orders. Our pharmacists also perform a drug utilization review in which they cross-check every prescription against the customer's submitted information for drug, disease and allergy interactions.

Over-the-counter medicines. We offer approximately 90 different classes of over-the-counter medicines, including Western medicines and Chinese medicines, for treatment of common diseases.

Consumer healthcare and personal care products. We offer approximately 160 types of personal healthcare products, including a variety of healthcare supplements, vitamins, minerals and dietary products, skin care, hair growth, beauty products and cosmetics and seasonal merchandise.

Private-label and exclusive products

We distinguish our retail drug stores from other chain pharmacies, in part, through our private-label products. We sell personal healthcare products under our private-label brand names, such as 妮可兒 (Nikeer) and 一致 (Accord), which provide a cost-effective alternative for consumers that offers the safety and effectiveness of comparable branded pharmaceutical products but at a lower retail price.

BUSINESS

We launched our first private-label products in 2006, and since then, our private-label lines have increased to over 207 products, covering most of the categories of over-the-counter products we offer. We intend to increase the sales of our private-label products in the future because they generally provide higher margins. The manufacture of all of our private-label products is outsourced to third-party manufacturers. Our manufacturing division in our other business operations does not supply to our retail stores any of the private-label products.

Exclusive products, which are provided by suppliers to us at preferential procurement prices, are available only in our retail drug stores in certain selected provinces. We launched our first exclusive products in 2006, and since then, our exclusive product lines have increased to over 608 products to date.

Pricing

We generally set the retail price of our products for our retail pharmacy operations based on the cost-plus method, including the cost of purchasing merchandise plus a standard mark-up for our operating costs. However, a portion of the pharmaceutical products that we sell through our retail pharmacy operations are, nonetheless, subject to price controls in the form of fixed prices or price ceilings. From time to time, the PRC Government will include new medicines in the Medical Insurance Catalog and adjust prices or set ceilings for the retail prices of such medicines to end-users. See "Financial Information — Factors Affecting Our Results of Operations — Policies and regulations of the PRC pharmaceutical industry" and "Regulation — Price Controls".

Marketing and Promotion

Prior to 2007, the marketing departments of our retail pharmacy operations designed our regional promotions based on local demographics and market conditions. Our marketing department consists of 33 persons responsible for marketing strategies. Since 2007, marketing and promotion activities have been conducted by our head office, which allows us to centralize our marketing and promotion activities. We run advertisements periodically in selected newspapers, as well as on billboards and seating areas of public transportation systems, to promote our brand and the products carried in our retail drug stores. In addition, we have joint marketing and promotion programs with our product suppliers and manufacturers, which primarily consist of gift promotions, featuring customized design packaged products, in-store product sampling and displays and periodical special discounts.

Distribution

Our retail drug stores are supported by our pharmaceutical distribution operations across China which facilitate the warehousing and delivery of products for those stores. Our suppliers deliver our retail products to our local logistics facilities, from which we then distribute the products to our retail drug stores.

Information Management

Each of our directly owned and franchise retail drug stores is equipped with a computer terminal that is connected to our centralized information management system via internet. All merchandise offered by our retail pharmacies is affixed with a unique bar-coded item number for its identification in the point-of-sale system which, in turn, is linked to a real time information system. When a cashier scans merchandise being sold, the relevant data is recorded instantly. Our information system generates a daily sales report, which enables us to quickly collect sales information, track and analyze inventory levels and sales trends and optimize retail store stock levels. We also use this system

to facilitate our category management decisions, fine-tune retail product selection and determine pricing, shelf space allocation and store replenishment triggers.

Currently, our retail drug stores and franchises which operate under the brand names 大德生 (Dadesheng) and 一致 (Yizhi) each uses different software for their respective information systems. We plan to implement a uniform information platform and data center for our retail pharmacy operations that standardizes the software used. We seek to fully integrate our merchandise selection, procurement, pricing, distribution and retail management on a single platform. We plan to upgrade our system and expect to complete the standardization by 2010. Upon such software standardization and system integration, we expect our retail information management system to become an intelligent information platform and portal, with the capacity to support the proposed expansion of our nationwide retail pharmacy operations. We also plan to share our logistics centers, inventory control and information management systems between our pharmaceutical distribution and retail pharmacy operations. We believe doing so will reduce our transportation, warehousing and logistics costs.

OTHER BUSINESS OPERATIONS

We also engage in the following businesses: (i) distribution and selling of laboratory supplies; (ii) manufacturing and distribution of chemical reagents; and (iii) production and sale of pharmaceutical products.

Chemical Reagents and Laboratory Supplies

We engage in the manufacturing and selling of chemical reagents and selling of laboratory supplies through our subsidiary, Sinopharm Chemical Reagent Co., Ltd.

Products

Our products include chemical, bio-chemical and diagnostic reagents, glassware supplies, laboratory equipment, apparatus and other laboratory products. These products are widely used in scientific research, environmental testing, chromatography, drug research and development, educational testing and fine and high-purity chemistry products. As of 31 May 2009, we had over 5,200 chemical reagents and over 6,000 laboratory products in our product catalog. In 2009, of our chemical reagent products, we manufactured over 40 chemical reagents products at our production facilities. Our other chemical reagent products and all of laboratory supplies are in each case manufactured by independent third parties. We have supplied chemical reagents and laboratory products to corporations, healthcare facilities, universities and other institutions for over 50 years.

We have an established position as a chemical reagents and laboratory supplies company in China. We sell our chemical reagents and laboratory supply products under our own and the third-party manufacturer's brand names. We have a number of chemical reagent and laboratory supply brands, including the following brands:

- 滬試 (Hushi)
- 沃凱 (Ourchem)
- 京試 (Jingshi)
- 申玻 (Shenbo)
- SCRC
- BOTEK

In addition to products sold under our own brand names, we are an authorized dealer of internationally recognized chemical reagent and laboratory supply brands such as Fluka, Fisher Scientific and Hach, as a result of our extensive and stable distribution channels and our insistence on GSP-qualified imports and high quality manufacturing.

Sales and marketing

We primarily sell our products in China. We have an extensive nationwide sales network, consisting of a direct sales force and third-party distributors in major cities in China. In addition to our head office in Shanghai, we have sales points in Beijing, Xi'an, Shenyang, Suzhou and Taicang. Taking advantage of convenient local services and superior brand recognition, we believe that we have established a leading sales network and service system in the PRC pharmaceutical industry.

Our sales and marketing team consists of 187 professional and experienced sales representatives responsible for product distribution and direct sales to end-users. We market our chemical reagents and laboratory supplies by establishing our own website as a platform for the sales and promotion of our products and publishing our own magazine through our subsidiary, Beijing China Reagent & Fine Chemicals Consulting Co., Ltd. In addition, we publish annually a reagents catalog that lists the specifications of our chemical reagents, which we distribute to our customers as part of our marketing strategy.

Our revenue recognition policy for the products sold in our other business operations segment is the same as that in our pharmaceutical distribution segment. See "— Pharmaceutical Distribution — Sales and Distribution Agreements".

Raw materials

The principal raw materials used for our chemical reagents are benzene, sulfuric acid, hydrochloric acid, nitric acid, sodium hydroxide, acetic acid, iodine, potassium hydroxide, sodium chloride and ethanol. We source our raw materials from independent third-party suppliers such as Fluka and Sigma. We store in inventory approximately 15 to 45 days of the raw materials used in the production of our chemical reagents. We enter into one-off spot contracts for the purchase of raw materials due to the nature of our business operations. Although we do not enter into long-term contracts with our suppliers, we have not experienced any supply shortages, and do not anticipate any difficulties obtaining the raw materials essential to our chemical reagent business.

Manufacturing

Production facilities. Currently, we have one manufacturing facility located in Taicang, China. It consists of three production lines, two of which are used for the manufacturing of organic and non-organic chemical reagents and one is used for the bottling of our chemical reagent products. To enhance our service to our customers, we also manufacture customized chemical reagents upon client's specific requests. Overall, we possess 102 manufacturing permits for chemical reagents.

Production capacity. Our manufacturing facility has an annual production capacity of (i) 640 tonnes of organic chemical reagents; and (ii) 320 tonnes of non-organic chemical reagents. Our bottling facility has a capacity to fill four million 500ml bottles per year.

Pharmaceutical Manufacturing

We are engaged in the research and development, manufacturing and sale of pharmaceutical products. We conduct these functions through three operating subsidiaries, namely Zhijun

Pharmaceutical, Guorui Pharmaceutical and Suzhou Zhijun Wanqing, at their manufacturing facilities located in Shenzhen, Huainan and Suzhou, respectively. Our manufacturing capabilities have allowed us to develop high-quality product lines, which we believe will result in the growing reputation of our own brands.

Products

In our pharmaceutical manufacturing operations, we primarily manufacture and sell our own non-patented generic pharmaceutical products that we sell under various brand names. We also manufacture and sell patented pharmaceutical products that we sell under our brand names. As of the Latest Practicable Date, we manufactured and sold 138 branded pharmaceutical products, primarily generic medicines. The vast majority of these products are prescription pharmaceuticals. For our branded generic products, we primarily focus on therapeutic areas such as anti-infectives, respiratory systems, cardiovascular systems and pain management. Our patented pharmaceutical products are in the areas of cough and medicine absorption. We also manufacture 25 chemical intermediates and APIs.

In addition, as of 31 May 2009, we had obtained the relevant approvals from the SFDA to manufacture and sell approximately 292 pharmaceutical products.

The following table sets forth the product categories of our major products, the number of products for each category and the major products in the product category:

Product category	Number of products	Major products
Zhijun Pharmaceutical:		
Antibiotics	53	Cefazolin Sodium for injection; Cefradine for injection; Cefuroxime Sodium for injection; Cefuroxime Axetil tablets and capsules; Cefoxitin Sodium for injection; Cefixime granules and capsules; Cefminox Sodium for injection; Ceftizoxime Sodium for injection; Ceftazidime for injection (with pre-added Arginine); Ceftazidime for injection; Cefotaxime Sodium for injection, Cefoperazone Sodium & Sulbactam Sodium for injection(2:1); Cefepime HCI for injection (with pre-added Arginine); Ceftriaxone Sodium for Injection; Cefonicid Sodium for Injection
Respiratory System	4	Compound Codeine Phosphate oral solution; Pseudoephedrine HCI & Codeine Phosphate oral solution; Ambroxol HCI oral solution
Others	9	Diclofenac Sodium S.R.; Paracetamol & Codeine Phosphate Tablets; Calcium & Vitamin C Chewable Tablets
Guorui Pharmaceutical:		
Antivirus	4	Ganciclovir for Injection; Potassium Sodium Dehydroandroandro grapholide Succinate for Injection; Ribavirin Dispersible Tablets;
Antibiotics	24	Netilmicin Sulfate for Injection; Clindamycin Phosphate for Injection; Azithromycin for Injection; Imipenem and Cilastatin Sodium for Injection; Spectinomycin Hydrochloride for Injection; Ceftriaxone Sodium for Injection; Cefotaxime Sodium for Injection; Cefoperazone Sodium and Sulbactam Sodium for Injection; Ceftazidime for Injection; Cefonicid Sodium for Injection; Cefpiramide Sodium for Injection; Cefradine for Injection; Cefminox Sodium for Injection
Cardiovascular and Cerebrovascular system	4	Betahistine Hydrochloride for Injection; Edaravone Injection
Pain relief	3	Lysine Acetylsalicylate for Injection;
Others	10	Metformin Hydrochloride and Glibenclamide Tablets (I); Pemirolast potassium tablets; Tiopronin Tablets; Sucralfate Tablets; Zoledronic Acid; Granisetron Hydrochloride for Injection; Fructose Sodium Diphosphate for Injection; Matrine for Injection
Suzhou Zhijun Wanqing:		
Antibiotics	26	Cefminox Sodium for Injection; Cefuroxime Sodium for Injection; Cefpirome Sulfate for Injection; Cefoxitin Sodium for Injection; Ceftriaxone Sodium for Injection; Cefonicid Sodium for Injection; Ceftazidime for Injection; Cefoperazone Sodium and Sulbactam Sodium for Injection; Cefoperazone Sodium for Injection; Cefotaxime Sodium for Injection
Pain relief	1	Oxoprofen
Others	25	Chemical Intermediate (including Cefoxitin Acid; Cefmetazole Acid; Cefixime) and API (including Cefminox Sodium; Cefuroxime Sodium; Cefathiamidine; Cefoxitin Sodium; Cefpirome; Cefamandole Nafate)

Sales and marketing

We primarily sell our pharmaceutical products in China. We sell substantially all of our products to local pharmaceutical distributors in China, including intersegment sales to our

pharmaceutical distribution and pharmaceutical retail segment. These distributors in turn distribute our pharmaceutical products to hospitals, clinics, retail pharmacies and other retail outlets or distributors. Although we currently distribute our pharmaceutical products primarily through local distributors in China, we plan to leverage our nationwide distribution network to facilitate our pharmaceutical manufacturing business, and to increase the proportion of our intersegment sales to our pharmaceutical distribution segment. In addition to our sales in China, we also have a small amount of export sales. We leverage our pharmaceutical sales and marketing experience gained from our distribution and retail businesses to launch and promote our products to our customers.

We generally enter into sales and purchase agreements that stipulate the volume and price of the products sold. The term of such sales and purchase agreements is generally one year. We provide credit for certain customers, and to determine the applicable credit terms and limits, we assess our customer's financial credit history. We reserve the right to terminate the purchase and sale agreements with our customers in the event of default.

We have a professional and experienced sales and marketing team. As of 31 May 2009, our sales and marketing department had approximately 219 sales and marketing representatives, with responsibilities for product sales and the provision of after-sales services. Most of our staff possesses an educational background in medicine or a related field.

Our sales and marketing team is in charge of our overall marketing strategy, our branding efforts and market research. We market our prescription pharmaceutical products by hosting in-person product presentations, conferences and seminars for physicians, other healthcare professionals and research scholars, and we also use healthcare magazines and newspapers to promote and generate awareness of our pharmaceuticals. With respect to our over-the-counter pharmaceuticals, we distribute flyers, display billboards in our pharmacies, engage in the use of electronic media and we also engage in sponsorship of charitable events. We are devoted to providing services to the community, and provide complimentary medicines and host educational seminars.

Raw materials

The principal raw materials used for our products are the necessary active ingredients of our pharmaceutical products, such as cephalosporin. We source raw materials, as well as packaging materials and supplemental materials, from various independent third-party suppliers in China. In addition, we may cooperate with suppliers to produce certain active ingredients used for the production of some of our pharmaceutical products, such as Cefuroxime Sodium. When we source raw materials from third parties, the purchase price for the relevant raw materials is based on the prevailing market price for such materials of similar quality. We generally keep a raw material supply that ranges from approximately 12 days to 35 days for raw materials used in pharmaceutical products, and 15 days to 45 days for raw materials used in chemical reagents.

Customary with what we believe to be standard practice in the industry, we do not have long-term contracts with any of our suppliers of raw materials. However, the majority of our raw materials have been readily available, and we have not experienced any major disruption in electricity or water supplies. From time to time, we have experienced shortages or price fluctuations of our raw materials, electricity and water supplies. However, such shortages or price fluctuations have not had a material adverse effect on our business.

BUSINESS

Manufacturing

We have approximately 1,935 employees in our pharmaceutical manufacturing operations. Of these employees, 305 are experienced engineers as of 31 May 2009. We have obtained all relevant approvals and permits for our manufacturing facilities for our pharmaceutical products. These approvals and permits include the pharmaceutical production permit, the GMP certificate, a business license and the requisite production approval. See "Regulation - Manufacturing of Pharmaceutical Products". We have obtained requisite licenses or permits for the sale of our manufactured pharmaceutical products from the SFDA at the national level that authorize our manufactured pharmaceutical products to be sold nationwide in China. We adhere to very stringent and closely monitored quality assurance and safety control processes in the manufacturing of our products. We are also expanding to the European market, and we aim to obtain European Union GMP approval by 2010 for our subsidiary Zhijun Pharmaceutical. Our manufacturing expertise and efficiency enables us to produce quality products cost-effectively and to sell such products at competitive prices.

In addition, from time to time, we outsource the manufacturing of some of our generic pharmaceutical and healthcare products to independent third-party manufacturers. We are therefore able to adjust our production capacity and our sales targets in response to market demands. The sales of products we outsourced to independent third parties for manufacturing accounted for approximately 2.9%, 6.6%, 7.3% and 4.3% of the total revenue of our pharmaceutical manufacturing operations in the years ended 31 December 2006, 2007 and 2008 and the five months ended 31 May 2009, respectively. We select our outsourced manufacturers based on a variety of criteria, such as their production capacity, quality control processes and reputation in the pharmaceutical manufacturing industry. All our outsourced manufacturers are bound by confidentiality obligations which prohibit them from revealing or using any confidential information relating to our products or production processes.

Production facilities. We currently have several GMP-certified production lines at our three manufacturing facilities in China located in Shenzhen, Huainan and Suzhou, respectively. See "— Properties". We have equipped our manufacturing facilities with world-class equipment and automated machinery imported from the U.S., Germany, Japan, Denmark and Italy. Together with our quality assurance and control systems, all of which comply with GMP requirements, we are able to carry out more than ten production lines available for powder injection, oral solution, oral solid dosage forms and API.

Production capacity. We have three subsidiaries engaged in pharmaceutical manufacturing at our three manufacturing facilities in Shenzhen, Huainan and Suzhou. The following table sets forth information on the designed capacity, actual production volume and utilization rates of our pharmaceutical manufacturing operations as of 31 December 2006, 2007 and 2008 and 31 May 2009:

Pharmaceutical Agent Production Unit	Delivery Form	Year ended 31 December 2006			Year ended 31 December 2007			Year ended 31 December 2008			Five months ended 31 May 2009		
		Designed Capacity[1]	Production Volume	Utilization Rate[2]	Designed Capacity[1]	Production Volume	Utilization Rate[2]	Designed Capacity[1]	Production Volume	Utilization Rate[2]	Designed Capacity[1]	Production Volume	Utilization Rate[2]
		(millions of units)	(millions of units)	(%)	(millions of units)	(millions of units)	(%)	(millions of units)	(millions of units)	(%)	(millions of units)	(millions of units)	(%)
Zhijun Pharmaceutical:													
Cephalosporins Antibiotics	Powder injection	80.0	109.9	137.4[3]	200.0	116.9	58.5	200.0	149.0	74.5	100.8	91.5	90.8
Cephalosporins Antibiotics	Oral solid dosage forms	100.0	98.1	98.1	500.0	175.4	35.1	500.0	289.3	57.9	208.3	214.9	103.2[3]
Respiratory System	Oral solution	20.0	19.4	97.0	30.0	16.7	55.7	30.0	17.2	57.3	12.5	5.1	40.6
Guorui Pharmaceutical:													
Antacids	Injection	1.3	-[4]	-[4]	1.3	0.4	33.1	1.3	0.6	46.6	0.54	0.49	90.7
Cephalosporins Antibiotics	Powder injection	43.2	7.6	17.6	43.2	22.0	50.9	43.2	10.1	23.4	18.0	3.28	18.2
General Antibiotics	Powder injection	40.0	24.7	61.6	40.0	37.5	93.8	40.0	36.5	91.3	16.7	20.58	123.2
Cardiovascular system	Powder injection	2.5	1.7	69.2	2.5	1.1	45.6	2.5	0.8	33.2	1.04	1.03	99.0
Cardiovascular system	Oral solid dosage forms	21.6	2.3	10.8	21.6	3.7	17.3	21.6	0.2	0.8	9.0	2.4	26.7
Anti-virus	Oral solid dosage forms	27.6	5.2	18.8	27.6	10.7	38.7	27.6	0.2	0.9	11.5	7.86	68.3
Suzhou Zhijun Wanqing													
Cephalosporins Antibiotics	Powder injection	30.0	7.1	23.7	30.0	20.7	69.0	100.0	26.2	26.2	41.7	12.8	30.6
Cephalosporins Antibiotics	Oral solid dosage forms	-	-	-	50.0	0.6	0.1	50.0	2.4	4.8	50	-[5]	-[5]
Cephalosporins Sodium Sterile API	N/A	80.0	10.5	13.1	80.0	36.9	46.1	136.0	109.7	80.7	66.7	37.8	56.7
Cephalosporins Sodium Oral solid API	N/A	-	-	-	30.0	-[4]	-[4]	30.0	9.7	32.3	12.5	4.2	33.3
Other API	N/A	-	-	-	20.1	1.3	6.7	20.0	0.8	4.1	8.3	0.8	9.2

(1) The designed annual capacity of each pharmaceutical agent production unit for the indicated period is measured by the daily (24-hour) production capacity for two shifts multiplied by 300 days per year, with respect to designed annual capacity and is measured as the daily (24-hour) production capacity for two shifts multiplied 125 days, with respect to designed capacity for the five-month period.

(2) Equal to the percentage of actual production volume over the designed production capacity for the indicated period.

(3) The utilization rate exceeded 100% because of production on an overtime basis, which included more than two shifts per day or 300 days per year.

(4) We did not produce such products in the period indicated due to a decrease of market demand and orders.

(5) We did not produce such products in the period indicated because we diverted relevant manufacturing facilities for the production of other products with larger market demand.

In order to meet the growing demand for antibiotic products in the PRC market, we plan to construct new manufacturing facilities for antibiotics products, which are expected to have an annual designed capacity of 500 million capsules and tablets and 100 million units in the form of granules and dried suspensions. Construction work is expected to be completed by the end of 2009. In addition, we also plan to upgrade our existing aseptic API and powder injection workshops by 2010 and 2011, respectively, to enhance our operating efficiency. The total construction costs and expenses for facility upgrades are approximately RMB81.7 million. We expect that we will finance the cost of upgrading existing and constructing new production facilities primarily from cash generated from our pharmaceutical manufacturing operations and bank borrowings. As of the Latest Practicable Date, we had no specific target for our acquisition of existing facilities from third parties.

INVENTORY

We actively manage and maintain our inventories to ensure cost-efficiency, quality control and the timely distribution, sales and manufacturing of our pharmaceutical and healthcare products. Our senior management is actively involved in setting inventory standards, and is continually seeking ways to further improve our inventory control.

Pharmaceutical Distribution

We manage our inventories with a focus on controlling our inventory holding costs, maintaining the variety of products available for our customers and ensuring the prompt delivery of our products to customers. We intend to conduct our inventory control through a centralized inventory management system. As of the Latest Practicable Date, five of our logistics hubs were integrated within one centralized inventory management system. We plan to integrate our entire network of distribution centers and logistics facilities into this centralized inventory management system by 2010.

We monitor the inventory levels of our operating subsidiaries by implementing a budgeted inventory turnover day and reviewing our inventory analysis reports. Our customers generally do not require us to maintain products at particular inventory levels as long as we are able to deliver products promptly. In addition, with the re-allocation of central medical reserve funds to our Company, we must maintain inventory at certain levels to meet emergency demands. Please refer to "— Pharmaceutical Distribution" for further information on the relevant arrangements between CNPGC and us. As of 31 May 2009, our inventories for emergency reserves had a total value of RMB132.2 million. We do not believe that the requirements of the PRC Central Government materially impact our inventory levels.

Retail Pharmacy

We manage our inventory to minimize inventory holding costs, ensure timely delivery of merchandise and maintain a variety of merchandise in our retail drug stores. We establish an inventory management target every year by reviewing our performance for past years and taking into consideration our data projections and market demographics. We perform monthly and ad hoc inventory counts in our stores and distribution centers, as well as perform daily inventory counts in stores for expensive merchandise. We monitor the shelf life of our pharmaceutical products by conducting a review six months prior to the expiration date of each pharmaceutical product. We utilize the data compiled to generate a monthly inventory analysis report, which is used to assess our inventory control measures and costs. We require that our store managers follow up on any inventory discrepancies discovered during each inventory count and report such results to the relevant operating subsidiaries.

Other Business Operations

We maintain a database for our inventory of raw materials, packaging materials and finished products. Our production facilities in Huainan, Shenzhen and Suzhou have a total gross floor area of approximately 97,000 sq.m. We carefully monitor our inventory levels to ensure adequate levels of raw materials and finished products. Our finished products generally have a shelf life that ranges from 360 days to 720 days for our pharmaceutical products, laboratory supplies and chemical reagents. We have an inventory provisioning method to value our inventories and to write off inventories when they become obsolete or damaged, or when their market value is below their carrying costs.

CUSTOMERS

Our five largest customers in our pharmaceutical distribution segment, which are also our top five customers overall, in the five months ended 31 May 2009 were Zhejiang Intmedic, Liaoning Pharmaceutical Foreign Trade Co., Ltd., Harbin Pharma, Shanghai Pharmaceutical Co., Ltd. and Nanjing Medical. For the years ended 31 December 2006, 2007 and 2008 and the five months ended 31 May 2009, our sales to our five largest customers accounted for approximately 3.0%, 3.1%, 3.2% and 3.3% of our total sales, respectively. In the same periods, our sales to our largest customer overall, Zhejiang Intmedic, accounted for approximately 1.0%, 1.0%, 1.1% and 0.9% of our total revenue, respectively.

None of our Directors, Supervisors, their respective associates or CNPGC, Fosun Pharma or Sinopharm Investment (the only shareholders of the Company, which, to the knowledge of the Directors, directly or indirectly own more than 5.0% of our share capital) or their respective Associates has any interest in any of the above mentioned customers.

Our trade receivables mainly represent the credit sales of our products to be paid by our customers and consist of accounts receivables and note receivables. As of 31 December 2006, 2007 and 2008 and 31 May 2009, our trade receivables were approximately RMB4,871.5 million, RMB6,110.5 million, RMB7,911.8 million and RMB9,347.9 million. We monitor the recoverability of our overdue trade receivables on a regular basis and when appropriate, provide for impairment of such trade receivables. For the years ended 31 December 2006, 2007 and 2008 and the five months ended 31 May 2009, our provision for doubtful trade receivables were RMB25.0 million, RMB22.4 million, RMB10.9 million and RMB17.7 million, respectively. For further details of our provisioning policy for trade receivables and the amount of our provisions, please see the sections headed "Financial Information — Critical Accounting Estimates and Assumptions — Impairment of receivables" and "Financial Information — Liquidity and Capital Resources — Working capital — Trade receivables".

Pharmaceutical Distribution

We have a broad customer base that includes hospitals and retail drug stores as well as other pharmaceutical distributors. Hospitals include general and specialty hospitals at the national, regional and municipal levels. Retail drug stores and other customers include national and regional retail pharmaceutical chain stores, independent pharmacies, community clinics and other healthcare institutions. Our retail customers include eight of the ten largest pharmaceutical retail chains in China, including China Nepstar Chain Drugstore, Cheng Da Fang Yuan Pharmaceutical Chain Co., Ltd., Hubei Tongjitang Pharmacy Co., Ltd., Chongqing Tongjunge Ltd., Kaixinren Drugstore, Guangdong Bencao Medicine Co., Ltd., Peace Drugstore and Shanghai Hua Shi Drugstore. Other pharmaceutical distributors include regional wholesalers or distributors at the provincial or municipal level which distribute pharmaceutical and healthcare products to end-customers. In addition, we offer a broad range of logistics and value-added services designed to enhance the operating efficiencies and competitive positions of our customers, thereby allowing them to improve the safety and effectiveness of healthcare services for their patients and consumers.

Retail Pharmacy

Our typical retail drug store customers are urban residents living in a major city in China. We periodically conduct qualitative customer surveys and these customer surveys improve our understanding of our market position and our customers' needs and preferences.

Other Business Operations

Our direct customers in our other business operations consist primarily of third-party distributors. Our pharmaceutical products were sold to over 7,900 hospitals, over 20,000 clinics and more than 50,000 pharmacies throughout China, as well as to entities in the Philippines, Thailand, Pakistan, Vietnam, Guinea, Sierra Leone, Nigeria, Malta, Hong Kong and Macau. In addition, we are in the process of registering our products in more than seven countries in Asia, Africa and South America. For the years ended 31 December 2006, 2007 and 2008 and the five months ended 31 May 2009, our export sales accounted for less than 1% of our revenues generated from other business operations segment.

SUPPLIERS

In the years ended 31 December 2006, 2007 and 2008 and the five months ended 31 May 2009, our purchases from our five largest suppliers for our pharmaceutical distribution operations, which are also our five largest suppliers overall, accounted for approximately 12.3%, 11.7%, 12.9% and 15.0% of our total cost of sales. Our purchases from our single largest supplier, Roche, accounted for approximately 4.0%, 3.5%, 3.5% and 3.9% of our total cost of sales in these periods.

None of our Directors, Supervisors, their respective associates or CNPGC, Fosun Pharma or Sinopharm Investment (the only shareholders of the Company, which to the knowledge of the Directors, directly or indirectly own more than 5% of our share capital) or their respective Associates has any interest in any of the above mentioned suppliers.

Pharmaceutical Distribution

We obtain pharmaceutical and healthcare products, as well as personal care products and medical supplies, from over 3,300 manufacturers. Our suppliers include 30 of the top 50 international pharmaceutical companies or their PRC affiliates or subsidiaries, which include Roche, Novo Nordisk, AstraZeneca, Pfizer, Boehringer-Ingelheim, Merck, and Eli Lilly, and 95 of the top 100 domestic pharmaceutical companies, such as Jiangsu Hengrui, Harbin Pharma, and North China Pharma. We believe that we have strong relationships with our suppliers, as we are the only national distributor of 162 pharmaceutical and healthcare products in China and the preferred regional distributor of 1,534 pharmaceutical and healthcare products. We are the preferred distributor for Boehringer-Ingelheim and the sole distributors for certain products of Pfizer, Bayer and Servier in China.

Retail Pharmacy

The development of our retail pharmacy operations depends to a significant degree upon our ability to offer consumers a broad selection of high-quality pharmaceutical products. As a result, our success in our retail pharmacy operations is dependent upon maintaining beneficial and stable supplier relationships for our retail pharmacy operations. We purchase our retail merchandise primarily from numerous third-party manufacturers and distributors, as well as to a lesser extent from our own pharmaceutical distribution and pharmaceutical manufacturing segments. Third-party suppliers include Bayer, Xian-Janssen Pharmaceutical Ltd., Shanghai Pharma and Shenzhen Kingworld. We also cooperate extensively with several leading cosmetics brands such as La Roche, Avene and Vichy, and provide retail space for their products in our stores.

We believe that alternative suppliers or alternative products are readily available for substantially all of the products we stock, and the loss of any one supplier would not have a material effect on our operations. Although we generally do not have long-term written contracts with our major suppliers, we have not experienced significant difficulty in maintaining reliable sources of supply, and we generally expect to be able to maintain adequate sources of supplies of pharmaceutical and other products sold in our retail pharmacies.

Other Business Operations

Our suppliers for our other business operations, which include Orchid Chemicals & Pharmaceuticals Ltd. and North China Pharma, Livzon Pharmaceutical Co., Ltd., Guangzhou Baiyunshan Pharmaceutical Co., Ltd. and Gosun Pharmaceutical Co., Ltd., are carefully screened. We require that our suppliers provide us with evidence that they have all licenses and permits necessary to conduct their operations, which may include business license, pharmaceutical production manufacturing permit, import registration certificate, GMP or other relevant licenses and any other related documents. We usually purchase our raw materials and supplies from various suppliers to enhance our bargaining power and to avoid over-reliance on a single supplier. We generally do not have long-term written contracts with our major suppliers for our other business operations. However, we believe that we have maintained good relationships with our suppliers, which enable us to procure raw materials and supplies used for our manufacturing operations in a reliable manner.

As of the Latest Practicable Date, we had not experienced any major interruptions in the supply of raw materials and other supplies for our pharmaceutical manufacturing operations. We believe that our raw materials and supplies purchased from our suppliers are fungible, and therefore, we do not anticipate significant difficulties in obtaining alternative sources of supply.

COMPETITION

The pharmaceutical distribution, retail pharmacy and manufacturing of laboratory supplies, chemical reagents and pharmaceutical products industries are highly competitive. We compete with domestic and foreign competitors, which vary widely by region and size of operations.

Pharmaceutical Distribution

We face a variety of competition in the distribution of pharmaceutical and health care products. According to the South Medicine Economics Research Institute, the pharmaceutical distribution market in China is highly fragmented, consisting of more than 9,500 distributors. In 2008, the three largest distributors in China accounted for approximately 20.0% of the PRC market in terms of total pharmaceutical distribution revenues, according to CAPC. According to CAPC, our market share, measured as a percentage of the total revenues of pharmaceutical distributors in China, was approximately 10.8% in 2008.

We compete with our competitors on the basis of type of customer served, breadth of product portfolio, service and delivery, logistics and value-added service programs, geographic coverage, credit terms, customer support and pricing. We differentiate ourselves from our competitors in China by the breadth of our product portfolio, our geographic coverage and the strength of the supply chain services we provide to our customers and suppliers, which include logistics and other value-added services. Most pharmaceutical distributors in China target a limited number of products or services and limit their operations to specific geographic regions. We compete on a nationwide level primarily with the two other large pharmaceutical distributors that have relatively significant market share in China. However, neither of these two large pharmaceutical distributors offer the entire breadth of our product portfolio, as one of the distributors focuses on imported pharmaceutical and healthcare products while the other focuses on non-hospital customers. In addition, we compete with other pharmaceutical

distributors on a regional or local level in the regions and local areas where these competitors engage in pharmaceutical distribution activities. When competing with regional and local competitors, we focus on attracting customers by offering our extensive distribution network, comprehensive product portfolio, stability and assurance brought by our scale and financial strength, as well as efficient and high-quality operation and service, which appeal to local customers. We also enhance our relationships with our local customers by assisting in their interaction with medical institutions across China. In addition, China's admission to the World Trade Organization in 2001 and subsequent changes in PRC laws and regulations have resulted in increased competition from foreign distributors that have entered the PRC market. These competitors have introduced successful business models and advanced logistics and information management systems, which may lead to increased direct competition.

Regardless of the degree or type of competition, to remain competitive we must continue to explore new customer relationships and business opportunities and further serve our existing customers by providing a comprehensive product portfolio, maintaining efficient inventory controls, offering flexible and reliable delivery services and providing competitive pricing.

Retail Pharmacy

According to Status Quo of Drug Supervision in China (中國的藥品安全監管狀況), there were more than 340,000 retail pharmaceutical stores in China in 2007. In each of the markets we operate, we compete with certain regional and local retail pharmaceutical chains, as well as independent pharmacies, supermarket and convenience chains, discount merchandisers, mail order prescription providers, membership clubs and internet pharmacies.

We compete principally on the basis of store location and convenience, merchandise selection, customer service and satisfaction, including offering customers the ability to pay by medical insurance card, private-label product offerings, prices, and our brand name. We believe that the continued consolidation of the retail pharmacy market and continued new store openings by chain store operators will further increase competitive pressures in this market. Although the geographical dispersion of our retail pharmacies enables us to offset the impact of competitive conditions in individual markets, we believe that more new store openings in certain of our target cities such as Beijing, Shanghai, Shenzhen and Guangzhou may intensify competition. Local regulations in such targeted cities may prohibit the opening of new retail drug stores within certain distances of an existing store, and where competitors have occupied many prime locations, we expect to face additional competition in terms of finding suitable new store locations if we expand in these cities.

Other Business Operations

We compete with several manufacturers and distributors that produce or sell, as applicable, the same type of laboratory supplies, chemical reagents and pharmaceutical products that we produce or sell. The identities of our key competitors vary by product and, in certain cases, different competitors may have greater or lesser market shares by region in China. We compete primarily on the basis of brand recognition, product efficacy, safety, reliability, availability and price.

QUALITY CONTROL

We maintain a highly stringent quality control system and devote significant attention to quality control for our pharmaceutical distribution, retail pharmacy and other business operations. Our quality control team is also responsible for ensuring that we are in compliance with all applicable regulations, standards and internal policies. Our senior management is actively involved in setting quality policies and managing internal and external quality performance.

Pharmaceutical Distribution

In our pharmaceutical distribution operations, we fully comply with all relevant PRC laws and regulations to ensure the quality of our operations. In addition, we obtained ISO9001 certification for quality control in 2007 for our distribution operations and logistics facilities. Further, we only use suppliers that have excellent credentials and product quality track records. Our quality control department at our head office and quality inspectors at each of our distribution centers and logistics facilities are responsible for implementing quality control measures in our pharmaceutical distribution operations. We also have climate-controlled warehouses to maintain suitable storage conditions for the quality and safety of pharmaceutical products.

We provide a pharmaceutical product examination report, or pharmaceutical report, for our different pharmaceutical products. We also provide "imported pharmaceutical products examination report" and "imported pharmaceutical product certification" for imported pharmaceutical products. When we receive products for distribution, we conduct spot inspections to examine such products in accordance with its pharmaceutical report. If the pharmaceutical products are qualified and have complete pharmaceutical reports, we will store them in our warehouse for distribution. If such products do not pass the examination, or if the pharmaceutical reports are incomplete, we will notify the supplier immediately without storing in our warehouse.

In addition, certain specialty medicines are stored separately in controlled settings and overseen by a specially-trained personnel. In order to comply with certain SFDA requirements, two specially-trained personnel generally escort the transport of such medicine. Expired medicine is stored in separate warehouses, and we immediately notify the relevant personnel to initiate the destruction procedures. Expired medicine is generally destroyed in two ways: (i) we return such medicine to where it originated; or (ii) we are given authorization to immediately destroy it in a controlled environment.

Retail Pharmacy

In our retail pharmacy operations, our quality control starts with procurement. In particular, we screen GMP-certified manufacturers in China and select a core group of suppliers to supply our private-label products after reviewing their product selection and quality, manufacturing, packaging, transportation and storage capabilities, as well as cost competitiveness. We conduct spot quality inspections of each batch of products we receive. We promptly replace our suppliers if they fail to pass our quality inspections. Since we maintain an extensive network of suppliers and standby suppliers, we believe we will not incur a material interruption to our business and operations if we choose to discontinue our cooperation with certain suppliers due to their unsatisfactory quality control record.

We place strong emphasis on the quality of the services rendered by our employees at all levels, including in-store pharmacists and store staff who directly interact with our customers. We regularly dispatch quality control inspectors to our stores to monitor the service quality of our staff. We take into account the feedback received during these inspections when determining employee promotions or bonuses. During the Track Record Period, we had not experienced any claim, litigation and arbitration or material adverse findings in investigation or audit by government authorities with respect to product liability, personal injury, wrongful death and negligent advice by our in-store pharmacist of our retail operations.

Other Business Operations

In our chemical reagents manufacturing operations, we have established quality control systems in accordance with all relevant national or industry guidelines. In addition, we also adhere to our internal quality control guidelines, which vary with different reagent products. We have obtained

ISO9001 certification for quality management systems in research and development and manufacturing of the chemical reagents, as well as the wholesale and retail distribution of chemical reagents and laboratory supplies, which indicates our compliance with internationally-recognized standards for quality control. We also impose quality control standards for our raw materials suppliers. We constantly inspect the raw materials and supplies used in our manufacturing process, and inspect and test internally manufactured products. We can replace any supplier that fails to pass such inspections.

In our pharmaceutical manufacturing operations, we have established quality control systems in accordance with the relevant PRC laws and regulations. In addition, we obtained ISO9001 certification for quality management systems in manufacturing APIs, powder injections, tablets and capsules, which indicate our compliance with internationally-recognized standards for quality control. Our quality control measures cover all aspects of our pharmaceutical manufacturing operations including design and construction of manufacturing plant and facilities, the installation of manufacturing equipment, maintenance of manufacturing equipment, procurement of raw materials and packaging materials, quality checks of raw materials, work-in-progress and finished products, monitoring adverse drug reactions and verification of documentation to comply with GMP standards and requirements. As a result, we have not experienced any material safety problems of our products reported by our customers or relevant government authorities or any material product liability or legal claims due to the quality of our pharmaceutical products and have not been subject to any adverse findings in any investigation or audit by any government authority during the Track Record Period.

In recognition of our products, services and brand, we have received several awards, including the first place award for Standardization of Chemical Reagents in 2007, given by the National Chemical Standardization Technology Committee, Chemical Reagent Branch, recognizing our intensive efforts to standardize 8-hydroyxquinoline, a chemical reagent commonly used for antiseptic and disinfectant purposes, as well as second place at the National Commercial Technology Progress Awards in 2006, given by the China General Chamber of Commerce, which recognized our ground-breaking efforts to integrate our chemical reagents statistical database and improve service quality. In addition, during the Track Record Period, we received three first grade awards and one second grade award from the National Technical Committee on Chemicals Standardization for our achievements in the research and development of chemical reagents.

OCCUPATIONAL HEALTH AND SAFETY

The PRC Government imposes a number of regulatory requirements on pharmaceutical companies with regard to employee safety. See "Regulation — Occupational Health and Safety" for a discussion of these requirements. We regard occupational health and safety as one of our important social responsibilities and have implemented safety measures at our production facilities to ensure compliance with applicable regulatory requirements. We have established a safety supervision department at each of our operating business entities. These safety supervision departments conduct periodic inspections of operating facilities to ensure that our pharmaceutical distribution, retail pharmacy and other business operations are in compliance with existing laws and regulations. We believe that safe practices are the only means to ensure employee safety. Thus, our safety supervision departments conduct regular training sessions for employees on accident prevention and management.

We conduct periodic inspections of our logistics facilities to ensure that our logistics operations comply with existing laws and regulations. We also conduct regular training sessions for employees on accident prevention and management. We have adopted combustible air detection, emergency spray equipment and volume controls to minimize the risk of injury at our distribution centers, manufacturing facilities, warehouses and laboratories. Some of the products and chemicals we distribute or manufacture are inherently dangerous, and we have adopted strict policies in accordance

with relevant national standards when handling such products. We have installed a safety monitoring system in each of our distribution centers, manufacturing facilities, warehouses and laboratories to regularly supervise our employees' activities.

We have also adopted a safe production development and accident prevention implementation policy in March 2008, which provides comprehensive guidelines on occupational health and safety. Among other things, the policy: (i) identifies the personnel and department responsible for accident prevention; (ii) details each employee's responsibility to prevent accidents and promote safety awareness; and (iii) requires safety performance reports on a regular basis.

We have implemented the Occupational Health and Safety Management System and obtained the OHSAS18001 certificate to improve our health and safety awareness, ability and operational skills in manufacturing our products. However, some of our business operations involve certain risks and hazards that are inherent in such activities and may not be completely eliminated by safety measures. These risks and hazards could result in damage to, or destruction of, properties or facilities, personal injury, environmental damage, business interruption and possible legal liability. See "Risk Factors — Risks Relating to Our Business Operations — Our operations are subject to operating hazards that may affect our operations and may not be fully covered by our insurance policies".

RESEARCH AND DEVELOPMENT

As of the Latest Practicable Date, we had one chemical reagent and 29 pharmaceutical products under development, six of which are being jointly developed through external collaborations and the remaining 24 are being developed through our internal efforts. The pharmaceutical products under development are mainly in the areas of antibiotics and respiratory systems. Subject to the granting of new approvals, we expect three new products to be launched in the PRC market by 2009. Our research and development activities for our pharmaceutical production operations mainly focus on the improvement of our existing therapeutic products and antibiotics for respiratory, cardiovascular, gastrointestinal and infectious diseases. We also conduct research and development of new products. For the years ended 31 December 2006, 2007 and 2008 and the five months ended 31 May 2009, we developed 16, six, four and six new pharmaceutical products, respectively, and have commenced commercial production and sales of these new products. As of the Latest Practicable Date, we had obtained all the relevant approvals for these new products developed by us. Further, we seek to obtain licenses for international pharmaceutical products that are developed in other countries but commercially unavailable in China.

As of 31 May 2009, we had 74 research staff who hold bachelor or higher degrees in science, of which 38 are experienced engineers. We enter into agreements with our research staff which provide that all relevant intellectual property belongs to us and all research staff are bound by confidentiality obligations with respect to research and development activities. We primarily conduct our research and development activities through our two operating subsidiaries, Zhijun Pharmaceutical and Guorui Pharmaceutical, both of which feature functional testing laboratories and advanced equipment with automation and cryogenic capabilities, as well as GMP-compliant trial production areas. In the years ended 31 December 2006, 2007 and 2008 and the five months ended 31 May 2009, our research and development expenses were RMB18.2 million, RMB24.6 million, RMB34.9 million and RMB11.8 million, respectively.

ENVIRONMENTAL MATTERS

Our pharmaceutical distribution and retail pharmacy operations are primarily governed by general environmental protection laws and related regulations. We must comply with relevant

provisions governing environmental protection and appraising of environmental impact as well as national and provincial standards of environmental quality established by various government authorities. For example, with respect to the development projects of our logistics facilities, we are required to carry out an environmental impact assessment and submit these assessment documents to relevant competent authorities for approval before we commence construction of these projects.

Our pharmaceutical manufacturing operations are governed by national, provincial and local environmental laws and regulations. The relevant laws and regulations applicable to pharmaceutical manufacturers in China include provisions governing air emissions, water discharge, prevention and treatment of sewage and exhaust fumes and the management and disposal of hazardous substances and waste. Manufacturers are also required to conduct an environmental impact assessment before engaging in new construction projects to ensure that the production processes meet the required environmental standards to treat wastes before the wastes are discharged. The primary wastes generated from our pharmaceutical manufacturing processes are air emissions, waste water, alcohol and organic waste, which are generated in compliance with all applicable environmental rules and regulations. PRC national and local environmental protection laws and regulations impose fees for the discharge of pollutants and, in cases where the pollutants have not been properly treated, fines for such discharge. The relevant environmental laws and regulations empower certain governmental authorities to shut down any enterprise that violates such laws and regulations through the discharge of pollutants.

During the Track Record Period, we carried out the relevant environmental impact assessments before commencing construction of our manufacturing facilities and have obtained all the required permits and environmental approvals for our manufacturing facilities. To ensure compliance with relevant laws and regulations on pollution control, we have established wastewater treatment and waste management facilities at our pharmaceutical production site to meet the requirements of the *Emission Standards of Pollutants for Pharmaceutical Manufacturers* (製藥工業污染物排放標準), which were effective on 1 August 2008. Our production facilities have obtained ISO9000 certification for our quality management system and ISO14001 certification for our environmental management system from the Universal Certification Service Co., Ltd., an organization authorized to issue quality-control certification, such as ISO certifications. In addition, our production facilities comply with all relevant environmental and manufacturing standards required by the GMP certification system.

We believe we are currently in compliance in all material respects with applicable national, provincial and municipal environmental laws and regulations and we have obtained all the relevant government approvals in relation to our operations. As of the Latest Practicable Date, we had not been the subject of any material environmental complaint or administrative penalties with respect to environmental violations. In this regard, our PRC legal counsel, Chen & Co. Law Firm, have confirmed that, during the Track Record Period, we complied with all applicable environmental laws and regulations in all material respects.

Our compliance with existing environmental laws and regulations has not had a material adverse effect on our financial condition and results of operations, and our management does not believe it will have such an impact on the future. We are not aware of any pending litigation or significant financial obligations arising from our current or past environmental practices that are likely to have a material adverse effect on our financial position. However, we cannot predict the impact that unforeseeable environmental contingencies or new or amended laws or regulations may have on us or our production facilities. In this regard, as PRC environmental compliance requirements continue to evolve, we may be required to make significant expenditures in order to comply with environmental laws and regulations that may be adopted or imposed in the future. We are also not able to predict our annual cost of compliance with respect to the environmental laws and regulations that may be adopted or imposed in the future. For further information on the environmental laws and regulations governing our operations, see "Regulation — Environmental Protection".

Our plans to address potential environmental laws and regulations that may be adopted in the future comprise the following: (i) empowering our legal and industrial departments to oversee and maintain our compliance with environmental protection policies; (ii) providing annual training to our staff regarding compliance with PRC environmental laws and regulations, and more frequent training, as required upon adoption of new environmental laws and regulations, and encouraging our staff to attend also environmental protection training sessions organized by the local environmental protection authorities; (iii) conducting weekly on-site inspections of our facilities; (iv) immediately reporting to our general manager any violation of PRC environmental protection laws and regulations; and (v) immediately reporting to and coordinating with the applicable PRC regulatory authorities in the event of environmental violations.

INSURANCE

We maintain property insurance policies covering our inventories, equipment and facilities in accordance with customary industry practice. We do not maintain product liability insurance or insurance covering potential liability relating to the release of hazardous materials as we believe maintaining product liability insurance for pharmaceutical products and insurance relating to the release of hazardous materials is not a common industry practice in China. In addition, the insurance policies of manufacturers generally cover potential product liability claims arising from the use of their pharmaceutical products that we distribute. Further, we do not maintain business interruption insurance or key-employee insurance for our directors as we believe it is not the normal industry practice in China to maintain such insurance. We carry occupational injury, medical pension, maternity and unemployment insurance for our employees, in compliance with applicable regulations. We consider our current insurance coverage to be adequate. However, we will continue to review and assess our risk portfolio and make necessary and appropriate adjustments to our insurance practice aligned with our needs and with industry practice in China.

PROPERTIES

Our corporate head office is located in Shanghai, PRC and occupy a total gross floor area of 3,690 sq.m. As of 30 June 2009, we occupied 35 parcels of land, of which we have obtained the land use rights certificates for 30 parcels. We have not obtained the land use rights certificates for the remaining five parcels. As of 30 June 2009, we occupied 310 buildings or units, of which we have obtained the building ownership certificates for 254 buildings or units. We have not obtained the building ownership certificates for the remaining 56 buildings or units. In addition, we leased 611 properties in the PRC as of 30 June 2009.

Jones Lang LaSalle Sallmanns Limited, an independent property valuer, valued the capital value of our real property interests attributable to our Company at approximately RMB810.6 million as of 30 June 2009. The text of the letter and the valuation certificates issued by Jones Lang LaSalle Sallmanns Limited in connection with its valuations are set out in Appendix V to this document.

Land Use Rights

As of 30 June 2009, we occupied 35 parcels of land with an aggregate site area of approximately 777,451 sq.m which are mainly used for storage and industrial purposes in the PRC. Of these parcels of land, except for certain portion of land parcels which need to change the title registration names, we have obtained land use rights certificates by way of land granting for 21 parcels, which have a total site area of approximately 589,139 sq.m and land use rights certificates by way of land allocated for nine parcels, which have a total site area approximately 66,593 sq.m. We have not

obtained land use rights certificates for the remaining 5 parcels, which have a total site area of approximately 121,718 sq.m. The details of these land parcels are as follows:

- 21 parcels of land, with an aggregate site area of approximately 589,139 sq.m, are granted land with land use rights certificates. According to our PRC legal advisers, Chen & Co. Law Firm, we can legally occupy, use, receive benefit from, transfer, lease, mortgage or otherwise dispose of the above land.

- We are applying to the relevant local authorities for the grant of land use rights for three parcels of land, with an aggregate site area of approximately 79,298 sq.m. The land use rights of the above land are contracted to be granted to us and the relevant land premium has been fully paid. According to our PRC legal advisers, Chen & Co. Law Firm, there is no legal impediment for our Company in obtaining the land use rights certificates after completing the relevant procedures for the grant of land use rights.

- Nine parcels of land, with an aggregate site area of approximately 66,593 sq.m, are allocated land with land use rights certificates. According to our PRC legal advisers, Chen & Co. Law Firm, we can legally occupy, use or with approval to transfer, lease, mortgage or otherwise dispose of the above land during the terms of holding the land use rights certificates. However, if we intend to transfer, lease or mortgage the above land, we should go through land grant procedures at the relevant land authority and pay additional land premium or land appreciation yields according to relevant laws and regulations.

- One parcel of land, with an aggregate site area of approximately 37,588 sq.m, has been listed in government planning policies and we cannot obtain the land use rights certificate. The land is mainly used for storage and is not material to our business operations. According to our PRC legal advisers, Chen & Co. Law Firm, we can not apply for the grant of land use rights at the present time but this will not affect our ability to occupy and use the land. We can apply for the land use right certificate only after the fulfillment of such policies. However, it is still uncertain when such government planning policies will be fulfilled. Therefore, as of the Latest Practicable Date, we had not applied for the land use rights certificate. We believe that the government planning policies will not adversely affect our operations.

- We are applying to the relevant local authority for the grant of land use rights for one parcel of vacant land, with an aggregate site area of approximately 4,832 sq.m. According to our PRC legal advisers, Chen & Co. Law Firm, we can legally occupy and use the land after completing the relevant procedures for the grant of land use rights. This vacant land is not material to our operations, we will try to obtain the land use right certificate before 31 December 2010.

Buildings

We currently occupy 310 buildings or units, with an aggregate gross floor area of approximately 425,100 sq.m, in the PRC. Of these buildings, except for certain portions of the buildings or units for which we need to change the names listed in the title registration, we have obtained building ownership certificates for 254 buildings or units, which have an aggregate gross floor area of approximately 376,794 sq.m. We have not obtained building ownership certificates for the remaining 56 buildings or units, which have an aggregate gross floor area of approximately 48,306 sq.m. The details of these buildings are as follows:

- We have obtained building ownership certificates and the corresponding granted land use rights certificates for 175 buildings or units, with a total gross floor area of approximately

250,016 sq.m. According to our PRC legal advisers, Chen & Co. Law Firm, except for certain portions of buildings or units for which we need to change the names listed in the title registration, we can legally occupy, use, receive benefit from, transfer, lease, mortgage or otherwise dispose of the above buildings or units.

- We have obtained a building ownership certificate and land use rights certificate for the leased land for five buildings, with a total gross floor area of approximately 4,916 sq.m. According to our PRC legal advisers, Chen & Co. Law Firm, we can legally occupy and use the buildings and the corresponding land.

- We have obtained building ownership certificates for 74 buildings or units, with a total gross floor area of approximately 121,862 sq.m, but have not obtained the land use rights certificates, as the corresponding lands are allocated land. According to our PRC legal advisers, Chen & Co. Law Firm, we can legally occupy, use or with approval to transfer, lease, mortgage or otherwise dispose of the above buildings or units and the corresponding land during the terms of holding the building ownership certificates. However, if we intend to transfer, lease or mortgage the above buildings or units, we should go through land grant procedures at the relevant land authority and pay additional land premium or land appreciation yields according to relevant laws and regulations.

- 25 buildings, with a total gross floor area of approximately 28,895 sq.m, are erected on the granted land which we have the land use rights certificate. These buildings are mainly used for industrial and storage purposes. We have not obtained the building ownership certificates for 24 buildings because we do not have relevant construction approvals. In March 2009, we acquired 75% of the equity interest in Suzhou Zhijun Wanqing. Before the acquisition, Suzhou Zhijun Wanqing had built 22 buildings prior to obtaining construction approvals. We also commenced construction of another two buildings of 926 sq.m. without applying for relevant approvals. We have decided to take remedial action to apply for ownership certificates of these buildings. The aggregate value of the 24 buildings is approximately RMB4.3 million. The use of these buildings is not in compliance with the relevant PRC laws and regulations. As a result, we may be subject to a penalty up to approximately RMB0.4 million and may be asked to demolish these buildings. We confirm the size of these buildings is relatively small and will not have any material adverse impact on our operations. For the remaining buildings, with a gross floor area of approximately 19,687 sq.m., we have obtained the relevant construction approvals and permits. According to our PRC legal advisers, Chen & Co. Law Firm, there is no legal impediment in obtaining the building ownership certificate.

- We have not obtained the relevant building ownership certificates and the relevant land use rights certificates for 31 buildings or units, with a total gross floor area of approximately 19,410.59 sq.m. According to our PRC legal advisers, Chen & Co. Law Firm, we can legally occupy and use these buildings after obtaining the building ownership certificates and land use rights certificates.

The abovementioned 56 buildings without title certificates are not material to our operations, and we will try to obtain the building ownership certificates before 31 December 2010.

As of the Latest Practicable Date, the following properties held by our subsidiaries were subject to encumbrances: a portion of one building and corresponding land located in Yangzhou, with an aggregate floor area of 3,411 sq.m. were subject to a mortgage with Bank of Communications Co., Ltd., Yangzhou branch.

Buildings Currently under Construction

As of 30 June 2009, we had a building, with an aggregate planned gross floor area of approximately 16,003 sq.m, that is currently under construction. We have obtained the relevant construction approvals and permits for one building which is erected on a parcel of granted land with a site area of approximately 10,421 sq.m. According to our PRC legal advisers, Chen & Co. Law Firm, we have signed the land use rights grant contract and the relevant land premium has been fully paid. There is no legal impediment in obtaining the land use rights certificate and building ownership certificate upon the completion of the building.

Leased Properties

As of 30 June 2009, we also leased 611 properties, with an aggregate gross floor area of approximately 190,699 sq.m, in the PRC. The lessors have provided the building ownership certificates or registrations with local authorities for 474 properties with an aggregate gross floor area of approximately 138,647 sq.m. The lessors have not provided the building ownership certificates or the evidence showing the owners' agreement to the leases or the lessors have registered the leases with the local authorities for the remaining 137 properties, which have an aggregate gross floor area of approximately 52,053 sq.m. Details of these properties are as follows:

- 474 properties with an aggregate gross floor area of approximately 138,647 sq.m. The lessors have provided the building ownership certificates or the evidence showing the owners' agreement to the leases or the lessors have registered the leases with the local authorities. According to our PRC legal advisers, Chen & Co. Law Firm, the leases are lawful, valid and legally binding.

- 137 properties with an aggregate gross floor area of approximately 52,053 sq.m. The lessors have not provided the building ownership certificates or the evidence showing the owners' agreement to the leases nor have the lessors registered the leases with the local authorities. We believe the leased properties without registered agreements are not material to our operations for the following reasons: (a) most of these leased properties are used for office, storage and retail purposes, it is convenient for us to find property nearby for replacement and relocation; (b) during the Track Record Period, we did not experience any incident where we were required to evict tenants from the leased properties; (c) the lessors of 106 properties have issued confirmation letters by which they undertake to indemnify any loss suffered by us that may result from such deficiency of title; (d) the profit generated by the operation of property for the retail pharmacy business during the Track Record Period was not material to our results of operations. According to our PRC legal advisers, Chen & Co. Law Firm, such leases may not be legal and valid but we will be indemnified by these lessors for any damages arising from this deficiency of title.

Sinopharm Investment has agreed under the Deed of Indemnity to indemnify the Company against any loss or liability suffered by any member of our Company in relation to, inter alia, defective title to the owned properties and non-registration of the leased properties of our Company. Please refer to the section headed "Connected Transactions" of the document for more details regarding the Deed of Indemnity.

EMPLOYEES

As of 31 December 2006, 2007 and 2008 and 31 May 2009, we had 10,572, 11,055, 12,259 and 14,449 full-time employees, respectively. The table below sets forth a breakdown of our employees by function as of 31 May 2009:

	Number of employees	% of total
Operations	4,144	28.7
Management, finance and administrative	1,910	13.2
Research and development and technical support	253	1.8
Sales and marketing	7,019	48.6
Others[1]	1,123	7.8
Total	**14,449**	**100.0**

(1) Others include office support staff, human resource staff, legal and compliance staff and maintenance and office security staff.

We have implemented a number of initiatives in recent years to enhance the productivity of our employees, which we hire through a competitive process. We conduct periodic performance reviews for our employees, and their salaries and bonuses are performance based. In addition, we have implemented training programs for various positions. We believe that these initiatives have increased employee productivity.

The remuneration package for our employees generally includes salary and bonuses. Employees also receive welfare benefits including medical care, housing subsidies, pension, occupational injury insurance and other miscellaneous benefits. As required by applicable PRC regulations, we participate in various employee benefit plans that are organized by municipal and provincial governments, including housing funds, pension, medical, maternity and unemployment benefit plans. We are required under PRC law to make contributions to the employee benefit plans at specified percentages of the salaries, bonuses and certain allowances of our employees, up to a maximum amount specified by the respective local government authorities where we operate our businesses from time to time. Members of the retirement plan are entitled to a pension equal to a fixed proportion of the salary prevailing at the member's retirement date. We also provide post-employment benefits to certain of our retired employees.

The total amount of our employee benefit expenses for the years ended 31 December 2006, 2007 and 2008 and the five months ended 31 May 2009 were approximately RMB562.7 million, RMB653.1 million, RMB891.8 million and RMB327.4 million, respectively.

Currently, all members of our work force are employed under employment contracts which specify the employee's position, responsibilities, remuneration and grounds for termination. All employees who are unable to work due to illness or disability are entitled to receive certain benefits during their period of absence from the workplace. In addition, the PRC Government requires us to provide work-related injury insurance for each of our employees. We and our subsidiaries have labor unions that protect employees' rights, help fulfill our and our subsidiaries' economic objectives, encourage employee participation in management decisions and assist in mediating disputes between us and union members. Each of our and our subsidiaries' operating units has a separate labor union branch. We believe that we have positive relations with our employees.

We provide extensive training for employees. The training is designed to strengthen staff commitment to qualify and improve staff knowledge in a number of important areas of our services, such as knowledge about our Company, products and customers service skills. For employees in our

pharmaceutical distribution operations, we provide an array of training programs and courses, such as: (i) logistics operations management; (ii) management and administrative training; and (iii) legal and administrative management. In addition, we believe that we offer one of the most extensive training programs in the retail industry. We provide training courses for our employees, in-store pharmacists, as well as management training for our regional managers and senior management officers at the head office, such as: (i) corporate culture, retail development plans and business process of our Company; (ii) emergency and safety management; (iii) basic pharmaceutical knowledge and GSP regulations and quality control regulations; (iv) selling skills, customer service, standards of service and evaluation criteria; and (v) product management. We believe that these programs have enhanced the productivity of our employees.

PERMITS, LICENSES AND APPROVALS

As of the Latest Practicable Date, we had obtained all requisite permits, licenses and approvals for our business operations. See the section headed "Regulation" for further information on permits, licenses and approvals applicable to our operations.

LEGAL PROCEEDINGS

As of the Latest Practicable Date, we were not a party to any material legal or administrative proceedings, and we are not aware of any threatened material legal or administrative proceedings against us. We may from time to time become a party to various legal or administrative proceedings arising in the ordinary course of our business.

During the Track Record Period, there were no personal injury, death or product liability claims that were brought against us for damages in connection with our business operations.

INTELLECTUAL PROPERTY

We rely on patents, trademarks and trade secrets as well as employee and third-party confidentiality agreements to safeguard our intellectual property. Our intellectual property rights are important to our business.

We rely on trademarks to protect the brands we use in our pharmaceutical distribution and retail pharmacy operations, as well as to protect the laboratory supplies, chemical reagents and branded generic pharmaceuticals, which are not protected by patents, we produce and sell in our other business operations. As of the Latest Practicable Date, we maintained 143 trademark registrations in China, including 國瑞 (Guorui), 一致 (Yizhi) and 大德生 (Dadesheng) and two trademark registrations in Hong Kong. As of the Latest Practicable Date, we also had 112 trademark applications filed and pending the approval of the PRC Trademark Office of the State Administration for Industry and Commerce, and one trademark application filed and pending the approval of the Hong Kong Trade Marks Registry. We also have been granted a non-exclusive license to use certain trademarks of our parent company, CNPGC, in our business pursuant to the Trademark License Agreement.

Under PRC law, we have the exclusive right to use a trademark for products and services for which the trademark has been registered with the PRC Trademark Office of the State Administration for Industry and Commerce. Trademark registration is valid for ten years, starting from the day the registration is approved. If we believe that a third party has infringed upon our exclusive rights with respect to any of our registered or licensed trademarks, we may, through appropriate administrative and civil procedures, institute proceedings to request the relevant authority for an injunction or to resolve the infringement through negotiation with the infringer. The relevant authority also has power to

impose fines, or confiscate or destroy the infringing products or equipment used to manufacture the infringing products.

As of the Latest Practicable Date, we held one design patent and two invention patents registered in China, which relate to improving the absorption and effectiveness of medicines. We have six invention patent applications pending the approval of SIPO. The invention patent applications are in relation to antibiotics, cough medicines and oral suspension medicines produced in our pharmaceutical manufacturing business. The validity period for our design patents is ten years and the validity period for our invention patents, if it is approved, will be 20 years, starting from the date the application was filed with the SIPO. We enjoy the exclusive right to exclude others from using, licensing and otherwise exploiting the patent in China.

We regularly submit patent applications for products and technologies that we have developed in order to actively protect our intellectual property rights. We also possess unregistered trade secrets, technologies, know-how, processes and other intellectual property rights. If our patents or trademarks are challenged, our brand name is damaged and/or our trade secrets become known by our competitors, there could be an adverse effect on our business. See "Risk Factors — Risks Relating to Our Business Operations — Third parties may infringe upon our intellectual property rights and other forms of protection under PRC law".

We do not consider any particular trademark or patent to be material to our overall business, since our principal business is the distribution, rather than the production, of medicines. Our pharmaceutical distribution operations do not require us to rely materially on the trademarks and patents that we use.

In addition to protecting our own intellectual property, our success also depends on our ability to minimize the risk that any of our products or operations infringes on the intellectual property rights of others. In each of our business segments, we follow a procedure under which our external trademark agent or legal counsel we engage will conduct a trademark clearance search before filing an application for the registration of a trademark. Similarly, in our other business operations, we follow a procedure under which our external patent agent or legal counsel we engage will conduct a patent clearance search for each product at the beginning of the product development process, and product development is only approved if the conclusion is that the proposed product would not infringe any third-party intellectual property rights uncovered in our searches. We also follow procedures to ensure that we do not engage in the sale of counterfeit pharmaceuticals. Our quality control department is responsible for checking the completeness of the certification and documentation provided by our suppliers before purchasing pharmaceutical products, and we will report to our senior management as well as the relevant local authorities if we discover any counterfeit pharmaceuticals. We believe that the risk of infringing third-party intellectual property can be effectively reduced by our vigorous adherence to these procedures. To date, we have not been sued on the basis of and have not undergone arbitration in respect of, nor have we received any notification from third parties that claim, any infringement of intellectual property of third parties or sale of counterfeit pharmaceuticals. Further, to date, we have not been the subject of any adverse finding in an investigation or audit by any governmental authorities in respect of any infringement of intellectual property of third parties or sale of counterfeit pharmaceuticals. However, despite our internal control procedures, the risk of infringing on third-party intellectual property cannot be eliminated entirely. See "Risk Factors — Risks Relating to Our Business Operations — We may face intellectual property infringement claims initiated by third parties" and "Risk Factors — Risks Relating to Our Business Operations — The existence of counterfeit pharmaceutical products in the PRC pharmaceutical retail market may damage our brand and reputation and have a material adverse effect on our business, financial condition, results of operations and prospects".