2010 Annual Report

CHINA MEDICAL SYSTEM HOLDINGS LIMITED

CMS

(Stock Code:867)

Contents

Corporate Information

Board of Directors

Executive Directors
Mr. LAM Kong
Mr. CHEN Hongbing
Ms. CHEN Yanling
Mr. HUI Ki Fat

Non-Executive Director
Ms. HOU Xiaoxuan

Independent Non-Executive Directors
Mr. CHEUNG Kam Shing, Terry
Dr. PENG Huaizheng
Mr. WU Chi Keung

Company Secretary

Mr. HUI Vincent Wing Sin, *HKICPA*

Authorized Representatives

Mr. HUI Vincent Wing Sin
Mr. LAM Kong

Audit Committee Members

Mr. WU Chi Keung (Chairman)
Mr. CHEUNG Kam Shing, Terry
Dr. PENG Huaizheng

Remuneration Committee Members

Dr. PENG Huaizheng (Chairman)
Mr. CHEUNG Kam Shing, Terry
Mr. WU Chi Keung

Nomination Committee Members

Mr. CHEUNG Kam Shing, Terry (Chairman)
Mr. LAM Kong
Dr. PENG Huaizheng
Mr. WU Chi Keung

Compliance Adviser

CMB International Capital Limited

Auditors

Deloitte Touche Tohmatsu
Certified Public Accounts

Principal Bankers

China Merchants Bank, Shenzhen Branch
Bank of Communications Co., Ltd.,
Hong Kong Banch
Industrial and Commercial Bank of China,
ShenZhen Branch
Hongkong and Shanghai Banking Corporation Limited

Registered Office

Maples Corporate Services Limited
PO Box 309
Ugland House
Grand Cayman, KY1-1104
Cayman Islands

Headquarters

6/F and 8/F, Building A
Tongfang Information Harbour
No.11 Langshan Road
Shenzhen Hi-tech Industry Park
Nanshan District
Shenzhen 518057
PRC

Principal Place of Business in Hong Kong

Unit 2106, 21/F
Island Place Tower
510 King's Road
North Point
Hong Kong

Branch Share Registrar in Hong Kong

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

Stock Code

867

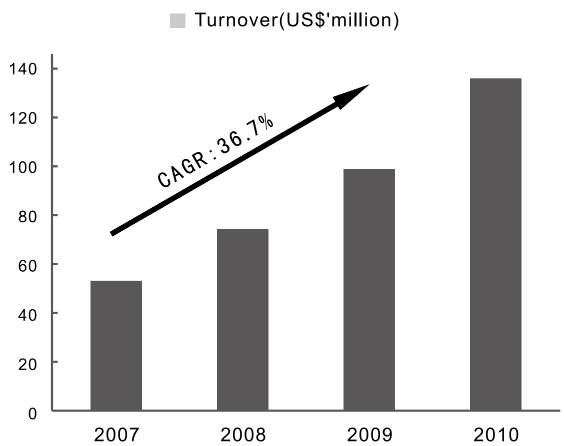
Company's website

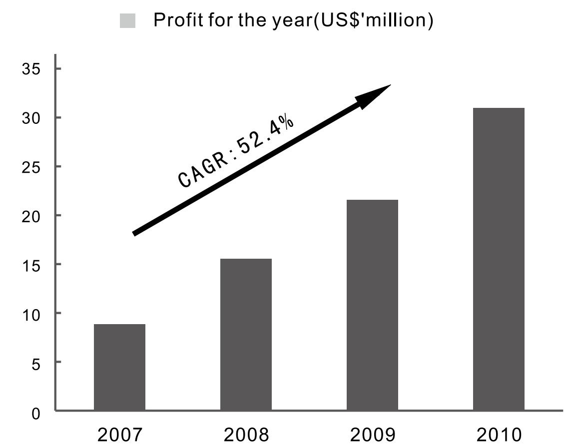
www.cms.net.cn

Financial Highlights

Consolidated Statement Of Comprehensive Income Highlights

	For the Year Ended 31 December				2007-2010
	2007	2008	2009	**2010**	CAGR
	US$'000	US$'000	US$'000	**US$'000**	
Turnover	51,747	72,600	96,454	**132,177**	36.7%
Gross profit	33,598	44,765	60,858	**78,102**	32.5%
Profit before taxation	10,346	19,535	26,926	**34,634**	49.6%
Profit for the year	8,674	15,048	20,830	**30,691**	52.4%
Net profit excluding listing expenses	11,447	15,048	20,830	**33,651**	43.3%
Profit attributable to owners of the Company	8,685	14,946	20,684	**30,587**	52.1%
Basic EPS (US$ cent)	0.993	1.582	2.186	**3.061**	45.5%





Consolidated Statement Of Financial Position Highlights

	As at 31 December			
	2007	2008	2009	**2010**
	US$'000	US$'000	US$'000	**US$'000**
Total assets	54,944	70,494	90,777	**223,207**
Total liabilities	13,100	17,773	36,843	**23,218**
Net assets	41,844	52,721	53,934	**199,989**

Performance Overview

In 2010, the Group's turnover was US$132.2 million (2009: US$96.5 million), an increase of 37.0% over the previous year; Profit attributable to owners of the Company was US$30.6 million (2009: US$20.7 million), an increase of 47.9% over the previous year. Basic earnings per share was US$3.061 cents (2009: US$2.186 cents), an increase of 40.0% over the previous year.

Chairman's Statement

Dear Shareholders,

On behalf of the Board of Directors, I would like to sincerely thank all our shareholders for their continued interest and unwavering support of China Medical System Holdings Limited (the "Company"or "CMS"). As Chairman of the Board I am pleased to present the Annual Report for the year ended 31 December 2010.

Results Overview

2010 was an important year and a significant milestone for the Company and its subsidiaries (the "Group"). During the year, we consolidated our strategies position as a marketing, promotion and sales service provider for prescription drugs in China. In September 2010, we successfully completed a transformation on the capital markets by transferring our listing platform from the Alternative Investment Market ("AIM") in London to the Main Board of the Hong Kong Stock Exchange ("HKEx").

Since listing in London in 2007, the Group has maintained continuous and stable growth, achieving a Compound Annual Growth Rate ("CAGR") of 36.7% and 52.4% for turnover and net profit, respectively, over the four years from 2007 to 2010. We were able to maintain this growth as a result of our sensible and flexible business strategy. In 2010, the Group achieved revenue of US$132.2 million (2009: US$96.5 million), a 37.0% increase over 2009. Profit attributable to owners of the Company was US$30.6 million (2009: US$20.7 million), which represents an increase of 47.9% year-on-year. Basic earnings per share was US3.061 cents (2009: US2.186 cents after adjustment for the resolution of the shareholders passed on 25 June 2010 and effective on 28 June 2010, each issued and unissued share in the share capital of the Company of a par value of US$0.10 into 20 new shares of a par value of US$0.005 each).

Business Review

The significant growth of the Group was achieved by our two well-defined, core business strategies - continuous introduction and development of products and sales network expansion.

Product In-licensing

In 2010, we introduced two new products - Bioflor and Exacin. During the year, we increased our efforts in product screening and engaged in discussions with domestic and international pharmaceutical enterprises over new products. In the past, our product introduction strategy focused primarily on products that were already being marketed in China - products which already had an import drug license or manufacturing license - which enabled us to generate sales as soon as we in-licensed them.

To increase the transparency in our product portfolio development and predictability and stability of our product development, the Group has considered three different product development strategies in products introduction in 2010.

Firstly, Rapid-growth products Strategy. The Group seeks products which are already available for sale in the China market and meet the selection criteria of CMS. This strategy has always been the pillar of our success, and the Group will continue to pursue this development strategy in the future.

Secondly, Long-term prospects product Strategy. Apart from products already available in the market, the Group will widen the product selection targets to those that require import drug license registration in China, which in turn will offer greater transparency in product development pipeline. These products will guarantee the sustainability of our product development from 2013. As at the time of writing, we have signed agreements for three products requiring product registration in China. Going forward, we will continue to in-license such products.

Thirdly, Strategy for the permanent control marketing rights of products. In order to increase the stability of the product rights, aside from managing the agency rights of products through contracts, the Group will also consider paying an upfront or licensing fee to obtain the permanent product or marketing rights in China for products with great market potential. The Group already owns the product rights of CMS024 (Tyroseuleutide) in China, which is used in the treatment of liver cancer and has huge potential market value. It is planned that the Phase III clinical trial of CMS024 will be initiated in the first half of 2011, and assuming a smooth clinical trial process, the product can be marketed in 2013. This product is expected to have a great impact on the Group's performance from then on.

The rapid growth in the Chinese pharmaceutical market and the Group's strategy to select products from the global product pool lends us considerable advantages in product availability and sustainability. This in turn gives a strong boost to the Group's development.

In addition to continued product line expansion, we have increased investment in the academic promotion of our products. While maintaining the steady growth of our two flagship products – Deanxit and Ursofalk, the Group has increased investment and effort in the promotional activity of new products introduced since 2007, with the prospect of minimizing the cultivation period and accelerating the development of new products. By doing so, the Group also reduced the reliance on our flagship products. For the year ended 31 December 2010, the sales turnover from our in-licensed products other than Deanxit and Ursofalk, contributed 31.7% of the sales turnover from total in-licensed products. As a result, turnover contributed from Deanxit and Ursofalk as a percentage of total turnover decreased to 66.7% in 2010 from 75.5% in 2009. These existing new products will become a major source of growth for the Group in the coming two to three years.

Network Expansion

In addition to product enhancement, the Group has continued to expand our professional sales and promotion team, refining and enhancing the structure and management of our promotion network. This year we recruited a large number of interns who are in the final year of their undergraduate or master's degree course in medicine or pharmacology. The elite from our internship programme are invited to join our team. We have refined our management system and extended our control in the sales network to improve its efficiency and drive in depth business development.

Besides from recruiting new staff to our network, the Group has continued to expand our geographic and hospital coverage. For the year ended 31 December 2010, our services reached over 7,100 hospitals. Our target doctors numbered over 120,000 with 44,000 of them having attended our drug promotion activities. These figures clearly reflected the progress that the Group has made in marketing and promoting our business during the year.

Hong Kong Listing

2010 was a milestone year for us as we transformed from a London-listed company to a Hong Kong-listed company. On 28 September 2010, we de-listed from the London AIM Board, on which the Group was floated three years ago, and successfully listed on the Main Board of HKEx. This move is significant for the development of the Group, and we believe that since our main business operations are in Mainland China, the Hong Kong listing is a positive step in raising the profile of the Group.

Following our listing in Hong Kong, we have placed even greater emphasis on investor relations, and by enhancing our interaction and communication with shareholders, we have enabled more investors to comprehend and familiarise themselves with the Group's business model. Through different methods we have improved the Group's transparency and created channels for investors to communicate smoothly with the Group. At the same time, we have continued to refine our management structure, strengthen our management system and cost control, and thereby effectively enhancing operation efficiency.

Dividend

The Board of Directors is pleased to recommend an final dividend of US1.3 cents per ordinary share of par value of US$0.005 (2009: US0.5 cents per ordinary share after adjustment for the resolutions of the shareholders passed on 25 June 2010 and effective on 28 June 2010, each issued and unissued share in the share capital of the Company of a par value of US$0.10 was sub-divided into 20 new shares of a par value of US$0.005 each) to shareholders whose names appear on the Registered of Members of the Company on Tuesday, 29 March 2011. As there was no interim dividend declared by the Group for the year ended 31 December 2010, the total divided for the year is US1.3 cents per ordinary share (2009: US1.0 cent per ordinary share after adjustment for the resolutions of the shareholders passed on 25 June 2010 and effective on 28 June 2010, each issued and unissued share in the share capital of the Company of a par value of US$0.10 was sub-divided into 20 new shares of a par value of US$0.005 each). The proposed final dividend will be paid on 4 April 2011 following approval at the Annual General Meeting ("AGM"). The register of members of the Company will be closed from 24 March 2011 to 29 March 2011 (both days inclusive) .

Outlook

Going forward, the Group will persevere in pursuing two core strategies in business development-introduction and development of products and sales network expansion. In terms of product development we will strive to maintain the steady growth of existing products and continue to in-license competitive products, adding to the transparency and visibility of our product development. In addition to maintaining the current long-term product agent strategy, the Group will also continue to explore acquisitions that will enable us to obtain the China market rights of products, thereby achieving more stable and sustainable product rights.

Regarding our network expansion, we will continue to recruit new staff, increase network coverage, establish new market segments, increase investment in network construction and improve flexibility in decision-making, to enhance market penetration.

In order to accelerate product introduction and network expansion, we will also consider mergers and acquisitions to achieve faster growth. We have set up a special working group to review acquisition opportunities in order to propel the Group's business to new heights.

2010 was a year of great significance for CMS, in which we achieved stable development, and through the Hong Kong listing secured a new and advantageous platform. We will continue to work hard, seize new opportunities and take practical measures in order to achieve even greater results!

Chairman
Lam Kong
Shenzhen China

24 February 2011

Management Discussion and Analysis

Business Review

Despite the challenging market environment in 2010, the Group achieved stable growth. For the year ended 31 December 2010, the Group's turnover was US$132.2 million (2009: US$96.5 million), an increase of 37.0% over the previous year. A net profit of US$30.7 million was recorded (2009: US$20.8 million), an increase of 47.3% over the previous year.

The noticeable achievement in the Group's performance resulted from the implementation of the two core strategies - the balanced progress of product introduction and development and network expansion.

Product Introduction

In addition to seven core in-licensed products, the Group successfully introduced another two products in 2010. We obtained the exclusive agency and distribution rights for Bioflor (Saccharomyces boulardii) in the Chinese market from Biocodex of France in January 2010 for a term of five years. Meanwhile, we successfully renewed the import drug license for Bioflor and obtained a new license at the close of 2010, facilitating promotion and sale of Bioflor in China. During the same period, we have signed two co-operation agreements with Asahi Kasei Pharma Corporation of Japan to obtain the right to promote and sell Exacin (Isepamicin Sulfate) imported under one-time permit in China. We are exploring long-term co-operation prospects with the manufacturer.

The introduction of the two products above was in accordance with our Rapid-growth product Strategy. The average of two products we assured shareholders which we will introduce each year represents products which are able to rapidly generate sales. The two products – Bioflor and Exacin – have already obtained import drug licenses and were sold in China before we in-licensed them. There is great market potential for these products as they are difficult to imitate with superior academic value. As soon as we started promotion and marketing the two drugs in China, they have contributed to the Group's sales.

We began to implement the Long-term prospects product Strategy in 2010 to increase the transparency of our products portfolio development and the visibility of future development. Apart from products available for sale in the China market, we also pay attention to introducing unregistered products requiring import drug registration in China. According to the relevant provisions of the State Food and Drug Administration ("SFDA"), the whole registration process of one new drug will typically be between two to five years. So it would take such products two to five years before they are able to contribute to the Group's sales. However, the introduction of in-licensing products requiring import drug registration approval can significantly facilitate sustainable development of the Group's products and business in the future. Between the end of 2010 and the beginning of 2011, the Group signed agreements for three products requiring import drug registration in China. These will take shape as candidates in the product pipeline of the Group. Details of these products are as below:

Budenofalk

Budenofalk is manufactured by Dr. Falk Pharma GmbH ("Dr. Falk"), and is the third product we have introduced from this drug manufacturing company. Budenofalk has the pharmaceutical composition patent which is used to treat Inflammatory Bowel Disease ("IBD") and Crohn's Disease. The indication is the same as Salofalk, the second product we in-licensed from Dr. Falk, but Budenofalk tends to treat more severe stages of IBD, and acts as an effective supplement to Salofalk. Recently, the number of IBD cases has increased significantly in China. According to statistics collected by the IBD division of the Chinese Medical Society of Gastroenterology, the estimated prevalence rates of ulcerative colitis and Crohn's Disease in China were about 11.6 out of 100,000 people and 1.4 out of 100,000 people respectively in 2008, with an upward trend in recent years. The Group signed a legally binding memorandum for Budenofalk with Dr. Falk on 15 December 2010. According to the memorandum, the Group gained the exclusive agency and distribution rights for Budenofalk in Mainland China and have been appointed as the registration agent of Budenofalk, assuming full responsibility for Budenofalk registration affairs in China. If Budenofalk can be successfully registered, CMS and Dr. Falk will use the memorandum as a basis to sign an exclusive agency and distribution agreement for five years, and will automatically extend for further five years if CMS comply with the terms of minimum purchase .

L-lysine Asescinat and Thiotriazolin

These two products are manufactured by Arterium Corporation ("Arterium"), which owns the substance patent or process patent. Arterium is one of the biggest pharmaceutical companies in Ukraine. The primary business of Arterium is to manufacture and sell various generic and novelty drugs.

L-lysine asescinat is used to treat swelling and pain, especially for the treatment of edema and injury to the brain and spinal cord, acute disorder of brain blood circulation and acute thrombophlebitis. The typical characteristics of cerebrovascular disease, which have great market potential in China, are high incidence, high mortality, high morbidity, high recurrence rate and high multiple complications. Thiotriazolin is used to treat chronic hepatitis arising from various causes, cirrhosis, liver failure, ischemic heart disease , myocardial infarction, angina and arythmia. In China, the incidence of cardiovascular disease and hepatobiliary disease is very high. The Chinese market size for cardiovascular drugs was approximately RMB60-70 billion in 2008 and expected to grow at an annual rate of 10%. More than 30 million people suffer from chronic hepatitis B in China but many of them have no recourse to treatment. As a drug to treat both cardiovascular disease and hepatobiliary disease, Thiotriazolin has large market potential in China. The Group signed a legally binding memorandum with Arterium on 10 January 2011 to gain the exclusive agency and distribution rights for the two products in China. We were appointed as the registration agent of the two products to assume full responsibility for their registration affairs in China. Once the two products are successfully registered, CMS and Arterium will, based on the memorandum, sign an exclusive distribution agreement for twelve years, and will automatically extend the agreement period if CMS comply with the terms of minimum purchase.

The Group currently offers Deanxit in the neurology field, XinHuoSu in the cardiovascular field, and Ursofalk and GanFuLe in the hepatology field. The introduction of L-lysine Asescinat and Thiotriazolin can effectively complement these three therapeutic areas for us, and our current expert network and product promotion experience in these three areas will benefit product sales and marketing following successful registration.

The above three in-licensed products still require three to five years to complete registration, and there is also the possibility that the registration will be unsuccessful. However, if the products are registered successfully, they will contribute significantly to the Group's sales in the future. These three products are not included in our commitment to introducing an average of two products per year into our portfolio.

In terms of Strategy for the permanent control marketing rights of products, the Group currently has CMS024 (Tyroserleutide), which is a product with independent intellectual property rights and one of the key products for the Group's future development. The registration of CMS024 as a new drug has been included in the special approval channel by the SFDA. Following completion of the explorative Phase II pump clinical trial, the Group held a successful roundtable meeting with the SFDA in October 2010, the primary purpose of which was to discuss the Phase III pump study design. As a result of the meeting, the Phase III study design of CMS024 was greatly simplified, with a reduction of the treatment group to 150 subjects, the trial is designed to observe CMS024's effect in control liver cancer recurrence after radical operation treatment, and the clinical trial designed to observe the Relapse Free Survival ("RFS") as the primary efficacy endpoint, using Overall Survival ("OS") as the secondary endpoint. It is expected that this Phase III clinical trial will begin in the first half of 2011. If the whole process proceeds smoothly, based on our expectations, CMS024 will be approved for market release three years ahead of our original estimate of 2016. The number of liver cancer patients in China accounts for over 50% of global cases. We believe that CMS024 will contribute greatly to the business of the Group from 2013 if it is successfully launched into the market as planned.

In addition to CMS024, the Group is still seeking and negotiating with manufacturers for the permanent China market rights of products with great potential to guarantee the sustainable development in the future.

Development of Existing Products

In 2010, while maintaining the steady growth of our two flagship products - Deanxit and Ursofalk - the Group has increased investment and effort in the promotional activity of our existing products. The existing products continued to make good progress this year as we focused on the academic and market characteristics of each product, and depending on the stage of individual products' development, we implemented target-orientated promotional strategies and plans.

(1). Products in Sustainable Growth Stage with Established Platform

Deanxit and Ursofalk were in-licensed in the early phase of the Group. The development of these two products is on a relatively established platform following nearly a decade of development. Our promotion strategy for these products is to support the brand building continuously and extend their geographic and depth of coverage. Against the backdrop of the overall growth in the Chinese pharmaceutical market, these products will maintain stable growth based on their current foundation.

Deanxit (Flupentixol and Melitracen)

Deanxit, our best-selling drug, was also our first in-licensed product. The main objectives for Deanxit in 2010 were to maintain its strong market position, continue to strengthen brand building through various promotional activities, and increase support to lagging regions in a bid to boost new growth. In 2009, Deanxit was included in the National Medical Insurance Catalogue - Class B, and in 2010, the product has progressively entered into the Provincial Medical Catalogue of developed areas, such as Jiangsu and Zhejiang, underpinning sales of the product. For the year ended 31 December 2010, Deanxit was sold to over 5,300 hospitals with sales reaching US$52.3 million, representing an increase of 17.7% over the previous year of US$44.5 million.

Ursofalk (Ursodeoxycholic acid)

Ursofalk is another key product for the Group. According to the Frost & Sullivan Report, Ursofalk accounted for 98.0% of the Ursodeoxycholic acid (“UDCA”) market in China in 2009. In 2010, the Group conducted more than 400 academic promotion activities, and also carried out on-going experts’ network maintenance and brand building. An example of our large-scale activities is the No.174 Falk Symposium which was held in Beijing from 27-28 August 2010 that attracted nearly 500 domestic and 300 international experts in the digestion field. The Symposium effectively established the image of the Group and its products. Ursofalk has been included in the National Essential Drugs List since 2009, following which we try to extend the range of hospital coverage to primary hospitals and strived to explore new opportunities with other potential hospitals. For the year ended 31 December 2010, Ursofalk was sold to nearly 3,000 hospitals and posted US$35.9 million in sales, representing an increase of 26.7% over the previous year of US$28.3 million.

(2). Products in Growth Stage

We have introduced an average of two additional products to our portfolio every year since late 2006, that is a total of seven new products up to 2010. Augentropfen Stulln Mono eye drops and XinHuoSu, which were introduced in 2007 and 2008 respectively, entered into the rapid growth stage after three to four years of investment and marketing cultivation. We have already laid the groundwork for the two products in terms of hospital coverage, expert network and doctor’s understanding and acceptance.

i. Products with Sound Market Base

Augentropfen Stulln Mono eye-drops (Escuilin and Digitalisglycosides Eye-Drops)

We refined our promotion strategy for Augentropfen Stulln Mono eye-drops in 2010. The new strategy focused on ocular asthenopia on the basis of senile macular degeneration. We conducted various promotional activities to strengthen doctors' product awareness and brand building. We also launched many clinical trials on ocular asthenopia to consolidate academic support. The new product positioning and strong academic promotion have enabled the product to maintain rapidly growth in this year. For the year ended 31 December 2010, the sales of Stulln was US$8.4 million, representing an increase of 37.4% over the previous year of US$6.1 million. The coverage of hospitals prescribing Stulln exceeded 2,000.

XinHuoSu (Nesiritide, Lyophilized Recombinant Human Brain Natriuretic Peptide, 'rhBNP')

2010 was an important year for XinHuoSu. During the year, XinHuoSu supported the publication of the Guidelines for Diagnosis and Treatment of Acute Heart Failure, the first such guideline in China, we also successfully renewed the drug license and completed a Phase IV clinical trial involving more than 2,000 patients. The Phase IV clinical trial not only confirmed the therapeutic effect and safety profile of XinHuoSu but also established doctors' confidence in its prescription, which played an important role in the successful sales of XinHuoSu. For the year ended 31 December 2010, XinHuoSu was sold to over 500 hospitals, and recorded sales of US$12.6 million, representing an increase of 73.4% over the previous year of US$7.3 million.

Exacin (Isepamicin Sulfate)

Prior to in-licensing into our portfolio, Exacin had already obtained certain degree of market coverage. Our main objective in 2010 was to ensure the smooth transition of the market and establish the high-end brand image of Exacin through academic promotional activities at various levels in order to lay the foundation for rapid development in the following year. For the year ended 31 December 2010, the sales of Exacin was US$10.6 million.

ii. Products Requiring Further Groundwork

Salofalk (Mesalazine)

Salofalk is used in the treatment of Inflammatory Bowel Disease ("IBD"), which is currently not widely recognised in China. Our main focus on this product in 2010 was to raise physicians' awareness and improve the diagnostic techniques of IBD, while constructing an expert network and supporting brand building for Salofalk. By inviting various foreign experts to lecture on the diagnostic techniques of IBD and organising the No. 174 Falk Symposium, we were able to establish a foundation for promoting Salofalk at a large scale in the future as a greater number of doctors came to understand the nature of IBD. For the year ended 31 December 2010, sales of Salofalk reached US$4.0 million, representing an increase of 118.7% over the previous year of US$1.8 million. The coverage of hospitals prescribing Salofalk was approximately 600.

Bioflor (Saccharomyces Boulardii)

Bioflor was in the process of renewing its import drug license when we signed the exclusive in-licensing agreement with Biocodex, and the sales of the product almost stopped at that time. In 2010, our emphasis on Bioflor was to complete the market transition, ensure the successful renewal of the import drug license, initiate an expert network and launch initial brand building. These activities were important for us in order to lay the foundation for large-scale market development in the future. For the year ended 31 December 2010, Bioflor recorded sales of US$1.3 million, and at the end of 2010, we successfully renewed the import drug license for Bioflor.

Both Salofolk and Bioflor have strong market potential and have grown rapidly. However, the process of market cultivation and the education of doctors for these two products are necessary due to the lack of market coverage. We believe that the two products will make greater contribution to the Group's business once the products' market groundwork is well established.

iii. Other Products

Cystistat (Sterile Hyaluronate Solution)

The treatment of interstitial cystitis by Cystistat is still not widely understood in China, thus Cystitat remains in the "market-entry" stage. The Group still needs to devote considerable resources to promote understanding of the product and indications. We primarily conducted clinical trials by co-operating with urology experts to improve doctors' understanding of the therapeutic effect and promoted the establishment of an expert network in 2010. For the year ended 31 December 2010, Cystistat recorded sales of US$0.7 million, representing an increase of 43.3% over the previous year of US$0.5 million.

GanFuLe

GanFuLe is our supplementary product in the liver cancer field. In 2010, we decided to forego the Northern China market and retained the exclusive right to promote and sell GanFuLe in Southern China, and focused on maintaining the stability and growth of the existing market. For the year ended 31 December 2010, sales of GanFuLe reached US$4.2 million, representing a decrease of 11.7% from last year of US$4.8 million due to us relinquishing the Northern China market. Sales of GanFuLe in other markets we retained actually increased.

Network Expansion

We continued to expand our marketing, promotion and sales network in 2010, and implemented an internship programme to attract talents. Many undergraduates and postgraduates nearing graduation from medicine and pharmacology colleges were hired as interns in our business regions, and the elite ones were invited to join our promotion team. The internship programme enables new employees to better understand and familiarise themselves with the Group's business and corporate culture, and also enable us to observe and select appropriate talents. As at 31 December 2010, more than 970 professionals served in our marketing, promotion and sales team.

Having obtained good results in 2010's internship programme, a large-scale recruitment of a new batch of interns is currently underway.

In addition to expanding our sales team, we also extended our geographical and hospital coverage. As at 31 December 2010, our marketing and promotion service covered 31 provinces and municipalities, including 100% of all provincial capitals and 87% of prefecture level cities. Our network serviced more than 7,100 hospitals, including 97.1% Class 3 hospitals and 38.4% Class 2 hospitals. About 120,000 doctors were targeted, while more than 44,000 participated in our activities in 2010.

While expanding the network, we continue to refine network management and the staff incentive mechanism, improving network construction to enhance the efficiency of network operations and promoting further in depth development of our business.

Outlook and Prospects

Our successful listing in Hong Kong in September 2010 provided new opportunities and new platform for the Group's business development. Based on the results of 2010, we will continue to strive for better results. On the one hand, we will step up the implementation of the three strategies for new product in-licensing and introductions. We will improve transparency, visibility and stability of products development. On the other hand, we will constantly expand the network, whilst strengthening self-management and market penetration abilities. We will also accelerate the Group's development through mergers and acquisitions by taking advantage of the Hong Kong capital market.

Financial Review

In reading the following discussion and analysis, please also refer to the annual report of the Group as shown in the audited financial statements and notes.

The Group and its subsidiaries' prepared audited annual reporting in accordance with international financial reporting standards, the basic financial performance are summarized as follows:

Turnover

Turnover represents the revenue we generated from the sale of in-licensed products and our in-house manufactured pharmaceutical products.

	2010		2009	
	US$'000	Weighted rate	US$'000	Weighted rate
In licensed product				
Deanxit	52,341	39.6%	44,468	46.1%
Ursofalk	35,879	27.1%	28,327	29.4%
Augentropfen Stulln Mono eye-drops	8,445	6.4%	6,146	6.4%
GanFuLe	4,219	3.2%	4,780	5.0%
XinHuoSu	12,576	9.5%	7,253	7.5%
Cystistat	738	0.6%	515	0.4%
Salofalk	3,989	3.0%	1,824	1.9%
Exacin	10,632	8.0%	-	-
Bioflor	1,266	1.0%	-	-
Others	602	0.5%	439	0.5%
	130,687	98.9%	93,752	97.2%
Other business				
In-house manufactured pharmaceutical products	1,490	1.1%	2,571	2.7%
In-house manufactured medical devices	-	-	131	0.1%
	1,490	1.1%	2,702	2.8%
	132,177	100.0%	96,454	100.0%

Turnover increased by 37.0% from US$96.5 million for the year ended 31 December 2009 to US$132.2 million for the year ended 31 December 2010. Our In-licensed product sales increased by 39.4% from US$93.8 million for the year ended 31 December 2009 to US$130.7 million for the year ended 31 December 2010. It was mainly due to an increase in the sales of existing products. Besides, we added two products to our portfolio, Exacin and Bioflor, in 2010. Our turnover of other business segments decreased by 44.9% from US$2.7 million for the year ended 31 December 2009 to US$1.5 million for the year ended 31 December 2010, primarily reflecting the competition from in-house manufactured products continued to intensify, resulting our in-house manufactured pharmaceutical products sales declined.

Cost of Goods Sold

Cost of goods sold increased by 51.9% from US$35.6 million for the year ended 31 December 2009 to US$54.1 million for the year ended 31 December 2010, primarily reflecting the growth in the Group's sales. For the purpose of the accounting treatment, part of the promotional expenses in relation to Exacin was included in the cost of goods sold.

Gross Profit and Gross Profit Margin

Gross profit increased by 28.3% from US$60.9 million for the year ended 31 December 2009 to US$78.1 million for the year ended 31 December 2010. Our gross profit margin slightly decreased from 63.1% in 2009 to 59.1% in 2010, primarily reflecting a change in the proportion of turnover accounted for by each of our in-licensed products. And partly because promotion expenses in relation to Exacin were included in the cost of goods sold for the purpose of accounting treatment.

Other Gains and Losses

Other income and gains of the Group decreased by 43.7% from US$0.7 million for the year ended 31 December 2009 to US$0.4 million for the year ended 31 December 2010, mainly reflecting a change in the foreign exchange rates.

Selling Expenses

The Group's selling expenses increased by 24.7% from US$24.8 million for the year ended 31 December 2009 to US$31.0 million for the year ended 31 December 2010, primarily reflecting increased marketing and promotion efforts with respect to our existing products and the additional expenses incurred for marketing and promoting the new products we added to our portfolio. Simultaneously, there was an increase in salaries and welfare for our marketing and sales staff as a result of increased sales and new sales staff. Our selling expenses as a percentage of our turnover decreased by 2.4% from 25.8% for the year ended 31 December 2009 to 23.4% for the year ended 31 December 2010 as we benefited from economies of scale.

Listing Expenses

The Group incurred total expenditure of approximately US$8.6 million for global offering in 2010, of which a total amount of US$5.6 million was charged to share premium account as share issuing expenses. The remaining US$3.0 million was charged to the statement of comprehensive income as listing expenses.

Administrative Expenses

The Group's administrative expenses increased by 27.9% from US$7.4 million for the year ended 31 December 2009 to US$9.5 million for the year ended 31 December 2010, mainly reflecting the expenditure increased because of the Hong Kong listing celebration. Benefiting from economies of scale, our administrative expenses as a percentage of our turnover decreased by 0.5% from 7.7% for the year ended 31 December 2009 to 7.2% for the year ended 31 December 2010.

Research and Development Costs

The Group did not incur research and development related costs for the year ended 31 December 2010 because we disposed our R&D operations in December 2009 following a strategic review of our business.

Finance Costs

The Group's finance costs increased by 58.2% from US$0.4 million for the year ended 31 December 2009 to US$0.6 million for the year ended 31 December 2010, mainly due to bank borrowings increased in 2010.

Taxation

The Group's taxation decreased by 35.3% from US$6.1 million for the year ended 31 December 2009 to US$3.9 million for the year ended 31 December 2010, primarily reflecting write-down of deferred taxation arising from unrealized intra-group transaction profits in inventories at year end, in accordance with International Financial Reporting Standards.

Profit for the Year

As a result of the above factors, our profit increased by 47.3% from US$20.8 million for the year ended 31 December 2009 to US$30.7 million for the year ended 31 December 2010. Compared with 2009, the group's net profit margin increased from 21.6% for the year ended 31 December 2009 to 23.2% for the year ended 31 December 2010. Excluding listing expenses, profit for 2010 was US$33.7 million and net profit margin was 25.5%.

Liquidity and Capital Resources

The Group funded our cash requirement mainly through cash generated from operations. During the reporting period, the cash and cash equivalent increased mainly because of funds raised from the global issue of shares and working capital increase. The following table is a condensed summary of our consolidated statements of cash flows:

	As at 31 December	
	2010	2009
	US$'000	US$'000
Net cash from operating activities	11,191	15,549
Net cash from (used in) investing activities	10,076	(16,616)
Net cash from (used in) financing activities	97,130	(4,022)
Net increase (decrease) in cash and cash equivalent	118,397	(5,089)
Cash and cash equivalent at beginning of the year	15,113	20,100
Cash and cash equivalent at end of the year	133,987	15,113

Net Cash from Operating Activities

For the year ended 31 December 2010,our net cash generated from operating activities was US$11.2 million, compared with US$15.6 million in 2009, a decrease of 28.0%, mainly due to the factor that some of our products were purchased on cash payment in 2010.

Net Cash from or used in Investing Activities

For the year ended 31 December 2010, our net cash generated from investing activities was US$10.1 million, compared with net cash used in investing activities of US$16.6 million in 2009, significantly increased by 160.6%, mainly reflecting most of pledged bank deposit raised in 2009 released in 2010.

Net Cash from or used in Financing Activities

For the year ended 31 December 2010, our net cash generated from financing activities amounted to US$97.1 million, compared with net cash used in financing activities of US$4.0 million in 2009, dramatically increased by 2,515.0%. It was mainly due to the proceeds from the company's global offering of shares.

Net Current Assets

	As at 31 December	
	2010	2009
	US$'000	US$'000
Current Assets		
Inventories	15,978	11,060
Trade and other receivables	49,314	32,794
Amount due from a jointly controlled entity	673	481
Held for trade investments	38	31
Tax recoverable	77	-
Pledged bank deposits	4,530	17,641
Bank balances and Cash	133,987	15,113
	204,597	77,120
Current Liabilities		
Trade and other payables	8,252	11,062
Bank borrowings - secured	4,261	16,517
Deferred consideration payables	1,198	838
Derivative financial instruments	48	145
Tax payable	2,709	1,226
	16,468	29,788
Net current assets	188,129	47,332

Inventories

The Group's inventory balances increased by 44.5% from US$11.1 million as at 31 December 2009 to US$16.0 million as at 31 December 2010, our average inventory turnover days increased from 87 days in 2009 to 91 days in 2010. It primarily reflects an increase in our finished goods stocks as a result of the increasing quantity for single purchases and inereasing sales.

Trade and Other Receivables

The Group's trade and other receivables increased by 50.4% from US$32.8 million as at 31 December 2009 to US$49.3 million as at 31 December 2010, primarily reflecting the growth of sales in 2010. Simultaneously, as strengthening of management of account receivables, our average trade receivables turnover days decreased from 73 days in 2009 to 71 days in 2010.

Trade and Other Payables

The Group's trade and other payables decreased by 25.4% from US$11.1 million as at 31 December 2009 to US$8.3 million as at 31 December 2010, primarily reflecting some of our products were purchased on cash payment. It also resulted a decrease in our average trade payables days from 60 days in 2009 to 21 days in 2010.

Capital Expenditures

The following table shows our capital expenditure during the report periods:

	Year Ended 31 December	
	2010	2009
	US$'000	US$'000
Purchase of property, plant and equipment	832	280
Purchase of land use right	2,918	-
Total	3,750	280

Debts

The following table shows the Group's debts during the report periods:

	As at 31 December	
	2010	2009
	US$'000	US$'000
Interest bearing bank borrowings and other borrowings	4,261	16,517

The Group's gearing ratio, calculated as bank borrowings divided by total assets, was 1.9% as at 31 December 2010, dropped significantly compared with 18.2% as at 2009, mainly reflecting the decrease of bank borrowings and the company's global offering of shares.

Market Risks

We are exposed to various types of market risks, including changes in interest rate risks, foreign exchange risks and inflation risks in the normal course of business. These risks are set out in the note 34 of financial statements.

Dividend

No interim dividend has been declared or paid during the year ended 31 December 2010 (2009: US$4.7 million). The Board resolved to declare the payment of a final dividend of US$14.9 million (2009: US$4.7 million), subject to the approval of the shareholders in the forthcoming AGM to be held on 29 March 2011.

Director and Senior Management

Executive Director

Mr. Lam Kong, aged 46, is the Chairman and Chief Executive Officer of our Group and was appointed as our executive Director on 18 December 2006. He acquired Shenzhen Kangzhe Pharmaceutical Co., Limited through his company over 15 years ago, building the business from a small company engaged in trading of pharmaceutical products to a leading pharmaceutical service company providing marketing, promotion and sale services. Mr. Lam is responsible for the creation, implementation and management of our development and growth strategy and the management of the overall operation of our Group. Mr. Lam possesses clinical experience and has over 15 years of experience in marketing, promotion, sale and other value-added services for pharmaceutical products in China. He received his bachelor's degree in medicine from Zhanjiang Medical College in 1986, the name of which was changed to Guangdong Medical College in 1992. Mr. Lam is a member of our Nomination Committee.

Mr. Chen Hongbing, aged 44, is the Chief Operating Officer of our Group and was appointed as an executive Director on 18 December 2006. He joined the Group in 1995 and has remained with our Group since then. Mr. Chen is responsible for the operation of our marketing, promotion and sale business and office administration. He had acquired about four years' clinical experience as a resident doctor with Nanjing Gulou Hospital from 1990 to 1994 prior to joining us in 1995. He graduated from Nanjing Medical College with a bachelor's degree in clinical medicine in 1990.

Ms. Chen Yanling, aged 40, is the Chief Financial Officer of our Group and was appointed as an executive Director on 18 December 2006. She joined the Group in 1995 and has remained with our Group since then. Ms. Chen is responsible for our Group's financial controlling, financial integration and financial management. She received her accountancy qualification in 1997 from the Ministry of Personnel of the PRC and from 1997 to 1999 studied and completed an MBA course recognised by the Administration of Foreign Experts Affairs of Guangdong Province.

Mr. Hui Ki Fat, aged 69, was appointed as our executive Director on 26 April 2007. He has also been a director of our subsidiary since 1999. He was a director and general manager of Jebsen & Company Ltd. in Tianjin, China for which he worked from 1968 to 1981 and from 1983 to 1998. Mr. Hui is the father of our Company Secretary and Chief Investor Relations Officer, Mr. Hui Vincent Wing Sin.

Non-Executive Director

Ms. Hou Xiaoxuan, aged 44, was appointed as our executive Director on 18 December 2006 and re-designated as a non-executive Director on 4 June 2010. Ms. Hou joined the Group in 1995 and has remained with our Group since then. She was primarily responsible for product regulatory affairs and office administration until the end of 2009. She was re-designated as a non-executive director on 4 June 2010. She is currently mainly involved in the overall strategic development of our business. Before joining us, she was a teacher at Kunming Medical College from 1989 to 1992 and was a human resources supervisor at Xinglong Enterprise (Shenzhen) Limited from 1992 to 1995. Ms. Hou received a bachelor's degree in clinical medicine from Kunming Medical College in 1989, a master's degree in accountancy from Renming University of China in 2000 and an EMBA from the Guanghua School of Management of Peking University in 2006.

Independent Non-executive Directors

Mr. Cheung Kam Shing, Terry, aged 48, was appointed as our independent non-executive Director on 18 August 2010. Mr. Cheung has more than 20 years' experience in securities broking, investment banking, fund management, private equity and other financial areas. He is currently a director of Greater China Corporate Consultancy & Services, being a professional services company providing corporate governance, accounting, tax and other corporate advisory services, since July 2010. The companies he served in after graduating from the University of Hong Kong in 1984 included Sanyo Securities (Asia) Limited, Fidelity International Investment Management Limited, Kerry Securities Limited, Sassoon Securities Limited, and Core-Pacific Yamaichi International (HK) Limited from 1984 to 2000. Mr. Cheung served as Managing Director at Culturecom Holdings Limited (a company listed on the Hong Kong Stock Exchange with stock code 0343) from 2000 to 2005. He later served as Managing Director of Nouveau Investment Group Limited from 2005 to mid 2010. Mr. Cheung received his bachelor's degree in social sciences from the University of Hong Kong in 1984 and his master's degree in science (financial economics) from the University of London in 1995. Mr. Cheung is the chairman of our Nomination Committee and a member of our Audit Committee and of our Remuneration Committee.

Dr. Peng Huaizheng, aged 48, was appointed as our independent non-executive Director on 4 May 2010. He is currently a partner of Northland Bancorp responsible for global life sciences industry and Asia/European investment opportunities. Prior to this, he was a director of corporate finance and head of life sciences at Seymour Pierce (an London-based investment banking firm), and prior to that Dr. Peng was a portfolio manager of global life science and technology funds at Reabourne Technology Investment Management Limited (now part of Close Brothers Asset Management Company). He also served as a non-executive director of China Medstar, which was an AIM-listed company, from 2006 until the company was delisted from AIM in 2008. He was a speaker at various international conferences in relation to investment in bio-technology industry. He received his bachelor's degree in medicine from Hunan Medical College (now Central South University Siangya School of Medicine, China) in 1984, his master's degree in medicine from Hunan Medical College in 1989 and his doctoral degree of philosophy in molecular pathology from University College London Medical School in London, UK in 1998. Dr. Peng is the chairman of our Remuneration Committee and a member of our Audit Committee and of our Nomination Committee.

Mr. Wu Chi Keung, aged 54, was appointed as our independent non-executive Director on 25 June 2010. Mr. Wu has more than 29 years of experience in financial audit and specialises in providing auditing and assurance services, financial due diligence reviews, support services for merger and acquisitions, corporate restructuring and fund raising engagements. Mr. Wu worked as an audit assistant at Touche Ross & Co. from 1980 to 1982 and as an accountant at Bylamson & Associates (Enterprises) Limited from 1982 to 1983. In 1983, he joined Kwan Wong Tan & Wong until it merged with Deloitte Touche Tohmatsu in 1997. Mr. Wu was a partner of Deloitte Touche Tohmatsu when he resigned in December 2008. Mr. Wu is currently the managing director of a family-owned private company in Hong Kong engaging in property and other investment activities, and an independent non-executive director of Jinchuan Group International Resources Co. Ltd engaging in the business of mining and mineral resources sector, the shares of which are listed on the main board of the Hong Kong Stock Exchange [stock code: 2362]. Mr. Wu is an associate of the Hong Kong Institute of Certified Public Accountants and a fellow member of the Chartered Association of Certified Accountants in the United Kingdom. Mr. Wu graduated from Hong Kong Polytechnic (now known as Hong Kong Polytechnic University) in November 1980 with a higher diploma in accountancy. Mr. Wu is the chairman of our Audit Committee and a member of our Remuneration Committee and of our Nomination Committee.

SENIOR MANAGEMENT

Dr. Ma Jonathan Zheng, aged 44, has been our Chief International Operations Officer since 2007. He joined the Group as an officer responsible for our international operations in 2005. He is primarily responsible for looking for and introducing new products to our Group. Earlier in his career, Dr. Ma worked at Pfizer in the United States. Dr. Ma received his bachelor's degree in statistics of the mathematics department from Peking University in 1988, a master's degree in science from University of Texas at El Paso in 1991 and a PhD from Yale University in 1995.

Dr. Wong Wai Ming, aged 50, has been our Chief Technical Officer since 2010. He first joined the Group in 2000 and then became the Chief R&D Officer in 2007. He is responsible for dealing with technical issues in introducing products and providing technical advice to our Group for selecting pharmaceutical products. Prior to this, Dr. Wong worked as manager of China pharma department for Jebsen Co. Ltd. He studied bio-chemistry and received his bachelor's degree in science and PhD from the University of Hong Kong in 1983 and 1993, respectively.

COMPANY SECRETARY

Mr. Hui Vincent Wing Sin, aged 38, has joined the Group and been our Company Secretary since 2007 and is also our Chief Investor Relations Officer. Mr. Hui is a member of the Hong Kong Institute of Certified Public Accountants and a member of the American Institute of Certified Public Accountants. Prior to joining the Group, he worked for Ernst & Young, Hong Kong. Mr. Hui received a bachelor's degree in biochemistry with nutrition and a master's degree in accounting and management science from the University of Southampton in the UK in 1994 and 1997, respectively.

Directors' Report

The Board of Directors of the Company is pleased to present the directors' report and audited financial statements of the Group for the year ended 31 December 2010.

Principal Activities

The Company is a holding company, the subsidiaries' principal activities are set out in the financial statements in note 40.

Results

The results of the Group for the year ended 31 December 2010 are set out in the consolidated statement of comprehensive income in page 39.

Reserves

Movements in reserves during the Reporting Period are set out in the consolidated statement of changes in equity in page 43 and note 32 to the financial statements.

Distributable Reserves

As at 31 December 2010, our company has distributable reserves of US$152.0 million available for distribution to our shareholders.

Use of Proceeds from the Company's Initial Public Offering

The Company issued 190,000,000 shares (including 20,000,000 shares via the exercise of the over–allotment option) in September 2010. The issue price was HK$5.06 per share, the proceeds amounted to approximately HK$961.4 million (equivalent to US$123.9 million). The net proceeds from the initial public offering after deducting share issuing expenses amounted to US$115.4 million. All the proceeds were received by the Company on 28 September 2010 and 25 October 2010 respectively. As at 31 December 2010, approximately US$23.0 million has been applied to intended uses as set out in the Company's prospectus, details of which are set out below:

1. Approximately US$0.7 million for continuing building up our marketing, promotion and sales network by hiring additional qualified and professional staff and expanding our hospital coverage and geographical reach;
2. The funds intended for constructing new training and conference centres to hold physician training, medical conferences and other promotion activities, as well as staff training to enhance the standard and professionalism of our promotion and sale services have not been used;
3. Approximately US$49,000 for changing, improving or upgrading both hardware and software of our information management systems so as to improve our management and control of our promotion network and business operations;

4. The funds intended for acquiring the exclusive in-licence rights to promote and sell pharmaceutical products in China and pursuing merger or acquisition opportunities of suitable pharmaceutical companies have not been used;
5. The funds intended for constructing a production plant for the manufacture of our in-house produced pharmaceutical products including CMS024 planned with following favorable clinical development of CMS024 have not been used;
6. Approximately US$10.7 million for providing funding for purchasing imported pharmaceutical products from suppliers, in order to fulfill increasing PRC market demand for our in-licensed products;
7. Approximately US$11.5 million for supplementing our working capital and other general corporate purpose.

As at 31 December 2010, the usages of proceeds did not differ from those disclosed in prospectus.

Property, Plant and Equipment

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

Property Interests

The Group's property interests as at 30 June 2010 were revalued by Vigers Appraisal & Consulting Limited, an independent property valuer, and the relevant property valuation report is set out in Appendix IV to the Prospectus. The total capital value of the Group's property interests as at 30 June 2010 set out in the aforesaid property valuation report was US$5,272,000, the net valuation surplus, representing the excess of market value of the properties over their book value, approximately US$674,000. Such revaluation surplus is not included in the Group's financial statements for the year ended 31 December 2010. Had the properties been stated at such valuation, an additional depreciation and amortization expense of approximately US$24,000 would have been charged against the consolidated statement of comprehensive income of the Group for the year ended 31 December 2010.

Share Capital

Movements in the share capital of the Company during the year are set out in note 30 to the financial statements.

Pre-emptive Rights

There are no provisions for pre-emptive rights under the Company's Articles of Associations(Articles) or the laws of the Cayman Islands which oblige the Company to offer new shares on a prorate basis to existing shareholders.

Purchase, Sale or Redemption of the Company's Listed Securities

The Company has not purchased, sold or redeemed any of its listed securities during the year end of 31 December 2010.

Directors

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

Executive Directors
Mr. LAM Kong (Chairman and Chief Executive Officer)
Mr. CHEN Hongbing (Chief Operating Officer)
Ms. CHEN Yanling (Chief Financial Officer)
Mr. HUI Ki Fat

Non-Executive Director
Ms. HOU Xiaoxuan

Independent non-executive Directors
Mr. CHEUNG Kam Shing, Terry
Dr. PENG Huaizheng
Mr. WU Chi Keung
Mr. Stuart Leckie (resigned on 2 August 2010)
Dr. Paul Harper (resigned on 4 May 2010)

Pursuant to Article 16.2 of the Articles of Association, any director appointed by the Board to fill a causal vacancy or as an addition to the Board shall hold office only until the next following AGM of the Company and shall then be eligible for re election at that meeting. Mr. Cheung Kam Shing, Terry was appointed by the Board on 18 August 2010 as an independent non-executive director. Accordingly, Mr. Cheung shall retire from his office at the AGM and, being eligible, will offer himself for re-election at the AGM.

Pursuant to Article 16.3 of the Articles of Association, any director appointed by the Company at a general meeting to fill a causal vacancy or as an addition to the Board shall hold office only until the next following AGM of the Company and shall then be eligible for re election at that meeting. Mr. Wu Chi Keung was appointed by the Company at the extraordinary general meeting held on 25 June 2010 as an independent non-executive director. Accordingly, Mr. Wu shall retire from his office at the AGM and, being eligible, will offer himself for re-election at the AGM.

Pursuant to Article 16.18 of the Articles of Association, at every AGM of the Company, one-third of the Directors for the time being (or, if their number is not three or a multiple of three, then the number nearest to, but not less than, one-third) shall retire from office by rotation provided that every Director (including those appointed for a specific term) shall be subject to retirement by rotation at least once every three years. Any Director appointed pursuant to Article 16.2 or Article 16.3 shall not be taken into account in determining which Directors are to retire by rotation. A retiring Director shall be eligible for re-election. Accordingly, Mr. Lam Kong and Ms. Chen Yanling will retire from their offices at the AGM and, being eligible, offer themselves for re-election at the AGM.

At the AGM, separate ordinary resolutions will be proposed for each of the re-elections of Mr. Lam Kong, Ms. Chen Yanling, Mr. Cheung Kam Shing, Terry and Mr. Wu Chi Keung. Details of these retiring Directors are set out in Appendix I to this circular.

Annual Confirmation of Independence

The Company has received from each Independent Non-executive Director an annual confirmation of his independence, and the Company considers such Directors to be independent in accordance with each and every guideline set out in rule 3.13 of the Rules Governing the Listing of Securities on the Stock Exchange of Hong Kong Limited (Listing Rules).

Biographical Details of the Directors and the Senior Management

The Biographical Details of the Directors and the Senior Management are set out on pages 19 to 21 of this Annual Report.

Directors' Service Contract

All the Non-executive Directors and Independent Non-executive Directors of the Company are appointed for a fixed period, and all three Independent Non-executive Directors were appointed for a one-year term. Their appointments are subjected to retirement from office by rotation and re-election at the AGM of the Company in accordance with the Company's Articles of Association.

Save as disclosed above, none of the Directors has or intend to enter into any contract of service with the Company or any of its subsidiaries which cannot be determinable by the employer within one year without payment of compensation (except for statutory compensation).

Management Contracts

No contracts concerning the management and administration of the whole or any substantial part of the business of the Company were entered into or existed during the reporting period.

Key Employee Benefit Scheme

Details of the key employee benefits scheme is set out in note 39 to the financial statements.

Directors' interests in Contracts of Significance

During the reporting period, none of the Directors had a material interest, whether directly or indirectly, in any contract of significance to the business of the Group to which the Company or any of its subsidiaries was a party.

Directors' Interests and Short Positions in Shares, Underlying Shares and Debentures of the Company and Its Associated Corporations

As at 31 December 2010, the interests or short positions of the Directors in the shares, underlying shares or debentures of the Company or any of its associated corporations (with the meaning of Part XV of the Securities and Futures Ordinance ("SFO")) which were recorded in the register required to be kept by the Company pursuant to section 352 of the SFO, or as otherwise notified to the Company and the Stock Exchange, pursuant to the Model Code for Securities Transactions by Directors of Listed Issuers as set out in Appendix 10 of the Listing Rules were as follows:

Name of Director	Name of Corporation	Nature of interest	Total number of Shares held (Note 1)	Approximate percentage of interest in the corporation
Mr. Lam Kong	The Company	Interest in controlled corporation	646,416,800(L) (Note 2)	56.52%
		Interest in controlled corporation	3,539,820(L) (Note 3)	0.31%
Mr. Chen Hongbing	The Company	Beneficial owner	15,712,620(L)	1.37%
		Interest in controlled corporation	40,000,000(L) (Note 4)	3.5%
		Beneficiary of a trust	3,539,820(L) (Note 5)	0.31%
		Derivatives	14,173,900(L) (Note 6)	1.24%
Ms. Chen Yanling	The Company	Beneficial owner	2,930,000(L)	0.26%
		Interest in controlled corporation	2,000,000(L) (Note 7)	0.17%
		Beneficiary of a trust	3,539,820(L) (Note 5)	0.31%
Ms. Hou Xiaoxuan	The Company	Beneficial owner	1,600,000(L)	0.14%
		Interest in controlled corporation	40,000,000(L) (Note 8)	3.5%
		Family interest	2,106,000(L) (Note 9)	0.18%
		Beneficiary of a trust	3,539,820(L) (Note 5)	0.31%
Mr. Hui Ki Fat	The Company	Interest in controlled corporation	5,276,660(L) (Note 10)	0.46%
		Beneficial owner	707,200(L)	0.06%
Mr. Chueng Kam Shing, Terry	The Company	Beneficial owner	320,000(L)	0.03%

Notes:
1. The letter "L" denotes Long positions in the Shares.
2. These Shares are held by Mr. Lam Kong through Treasure Sea Limited, a company wholly owned by him.
3. These Shares are held by Fully Profit Management (PTC) Limited, a company wholly owned by Mr. Lam Kong. Fully Profit Management (PTC) Limited is the trustee of the Key Employee Benefit Trust, (a discretionary trust established by our Company on 31 July 2009 for the Key Employee Benefits Scheme). Please refer to note5 below for further details.
4. These Shares are held by Mr. Chen Hongbing through Viewell Limited, a company wholly owned by him.
5. These Shares are held by Fully Profit Management (PTC) Limited acting as the trustee of the Key Employee Benefit Trust. The discretionary objects of the discretionary trust include Mr. Chen Hongbing, Ms. Chen Yanling and Ms. Hou Xiaoxuan and they are deemed to be interested in these 3,539,820 Shares. The references to these 3,539,820 Shares in respect of which Mr. Lam Kong is deemed to be interested in (as disclosed above) relate to the same block of Shares.
6. This represents the Existing Share Options.
7. These Shares are held by Ms. Chen Yangling through Great Creation Holdings Limited, a company wholly owned by her.
8. These Shares are held by Ms. Hou Xiaoxuan through Wide Harvest Limited, a company wholly owned by her.
9. These Shares are held by Mr. Jia Jinbin, the spouse of Ms. Hou Xiaoxuan, in respect of which Ms. Hou Xiaoxuan is deemed to be interested in.
10. These Shares are held by Mr. Hui Ki Fat through Archiever Development Limited, a company wholly owned by him.

Directors' Right to Acquire Shares or Debentures

At no time during the year was rights to acquire benefits by means of the acquisition of shares in or debentures of the Company granted to any Director or their respective spouse or minor children, or were any such rights exercised by them; or was the Company or any of its subsidiaries a party to any arrangement to enable the Directors, their respective spouses or minor children to acquire such rights in any other body corporate.

Substantial Shareholders' Interests and Short Positions in Shares, Underlying Shares and Debentures of the Company and Its Associated Corporations

As at 31 December 2010, the interest and short positions of the following shareholders (not being a Director of the Company) in the shares or underlying shares or debentures of the Company which would have to be disclosed to the Company and the Stock Exchange pursuant to Divisions 2 and 3 of Part XV of the SFO or were recorded in the register required to be kept by the Company pursuant to section 336 of the SFO were as follows:

Name of shareholder	Nature of interest	Total number of Shares held(Note 1)	Approximate percentage of interest in our Company
Martin Currie (Holdings) Limited (Note 2)	Interest in controlled corporation	79,724,960(L)	6.97%
Martin Currie Limited(Note 2)	Interest in controlled corporation	79,724,960(L)	6.97%
Martin Currie Inc.(Note 2)	Interest in controlled corporation	74,493,760(L)	6.51%
China Fund, Inc(Note 2)	Interest in controlled corporation	72,353,760(L)	6.33%
Martin Currie Investment Management (Note 2)	Interest in controlled corporation	5,231,200(L)	0.46%

Notes:

1. The letter "L" denotes Long positions in the Shares.
2. The China Fund, Inc. is a closed ended, non-diversified management investment company registered under the US Investment Company Act of 1940 and incorporated in Maryland, the United States. Martin Currie Limited, a company incorporated in New York, the United States, is the investment manager to the China Fund, Inc.Martin Currie Inc. is wholly owned by Martin Currie Limited, a company incorporated in Scotland, the United Kingdom. Martin Currie Investment Management is also wholly owned by Martin Currie Limited, a company incorporated in Scotland, the United Kingdom. Martin Currie Limited is a wholly-owned subsidiary of Martin Currie (Holdings) Limited, which is a company incorporated in Bermuda.

Connected Transactions

Key Employee Benefit Scheme

Details of the key employee benefits scheme is set out in note 39 to the financial statements.

Existing Share Options

Details of the existing share options are set out in note 31 to the financial statements.

Directors' and Management Emoluments

Particulars of directors' emoluments and the five highest paid individuals in the Group are set out in notes 8 to the financial statements.

Major Customers and Suppliers

In 2010 the percentage of sales attributable to the Group's five largest customers during the year was approximately 24.7% of the Group's total sales. Sales to the top customer accounted for approximately 6.8% of the total sales during the year.

Purchases from the Group's five largest suppliers in aggregate represented approximately 93.3% of the Group's total purchases during the year. Purchase from the top supplier accounted for approximately 39.0% of the total purchases during the year.

None of the Group's directors, director of the contacts, the shareholders had an interest in supplier or customer.

Corporate Governance

Report for the corporate governance principles and practices adopted by the Company are set out on pages 31 to 36 of this report.

Sufficiency of Public Float

According to publicly available information and as far as the Directors were aware, as at the date of this report, there was a sufficient public float of the Company's issued shares as required under the Listing Rules.

Non-competition and Indemnity Agreements

The Company entered into Deed of Non-competition with Mr. Lam Kong and his wholly owned company—Treasure Sea Limited ("Treasure Sea") on 14 September 2010. Mr. Lam Kong and Treasure Sea Limited jointly undertook not to carry on businesses that are in competition with the Company's businesses.

Mr. Lam Kong and Treasure Sea Limited stated that they complied with the relevant clauses of non-competition agreements. They did not engage into businesses that are in competition or maybe compete with the business of the Company and any of its subsidiaries. They did not directly or indirectly hold any businesses' interest that is in competition with the business of the Company and any of its subsidiaries as well.

The independent non-executive Directors have reviewed the compliance issue of the Deed of Non-competition with Mr. Lam Kong and Treasure Sea Limited for the period from 28 September 2010 to 31 December 2010, and reviewed relevant business information provided by the Company. The independent non-executive Directors were of the opinion that Mr. Lam Kong and Treasure Sea Limited complied with the relevant terms of the Deed of Non-competition during the period from 28 September 2010 to 31 December 2010 and did not cause any competition with the Company. The Board of Directors operated and managed the Company's businesses independently in the interests of the Company and its shareholders as a whole.

Donations

The Company made no donation in any form for the year ended 31 December 2010.

Compliance with the Corporate Governance Code

During the period from 28 September 2010 to 31 December 2010, except for a deviation from the Code provision A.2.1 in respect of the roles of chairman of the board and Chief Executive Officer should not be performed by the same individual, the Company has complied with the code of Best Practice as set out in Appendix 14 of the Listing Rules. For details, please see page 31 of this annual report.

Competing Interests

None of the Directors or management shareholders of the Company and their respective associates (as defined in the Listing Rules) has an interest in a business which competes or may compete with the business of the Company or has any other conflict of interest with the Company during the reporting period.

Audit Committee

The details of Audit Committee are set out in page 33 to 34 of the corporate governance report.

Auditors

The Company has appointed Deloitte Touche Tohmatsu as auditors since the listing of the Company on the Main Board of the HKEx on 28 September 2010.The financial statements in the annual report for the year have been audited by Deloitte Touche Tohmatsu. A resolution will be submitted at the AGM of the Company to re-appoint Deloitte Touche Tohmatsu as auditor of the Company.

Post Balance Sheet Event

There was no significant post balance sheet event after 31 December 2010.

Corporate Governance Report

The Company is committed to upholding high standards of corporate governance and has adopted sound governance and disclosure practices. The Company believes that maximizing long-term shareholder value by increasing the Group's accountability and transparency through improving the level of corporate governance.

Corporate Governance Practices

For the period between 28 September 2010 to 31 December 2010, the Company has adopted all the relevant provisions contained in the Corporate Governance ("CG") Code set out in Appendix 14 of the Listing Rules and has complied with all other provisions of the CG Code, except for a deviation from the Code provision A.2.1 in respect of the roles of Chairman and Chief Executive Officer which should not be performed by the same individual.

Directors' Securities Transactions

The Company adopted the Model Code for Securities Transactions by Directors of Listed Issuers (the "Model Code") as set out in Appendix 10 of the Listing Rules as the code of conduct for Directors' securities transactions. Having made specific inquiries in relation to the compliance with "Model Code" for securities transactions by Directors, the Company confirmed that all the Directors have complied with the relevant standards for securities transactions by directors set out in the Model Code during the period from 28 September 2010 to 31 December 2010.

Operation of the Board

In accordance with good corporate governance principles, the Board convened regular and interim meetings in accordance with legal procedures and complied strictly with relevant laws, legal regulations and the Articles of Association of the Company in the exercise of its authority, with an emphasis on protecting the interests of the Company and its shareholders.

The role and responsibilities of the Board broadly cover reviewing and approving corporate mission and broad strategies; overseeing and evaluating the conduct of the Group's businesses; identifying principal risks and ensuring the implementation of appropriate measures and control systems to manage these risks; and reviewing and approving important matters such as financial results, investments and divestments and other material transactions.

The Company has established three committees, namely, the Audit Committee, Nomination Committee and Remuneration Committee, which mainly comprised of Independent Non-executive Directors and responsible for overseeing particular aspects of the Group's business, and to provide the Group with recommendations for improvements. Please see below for the work scope of these three committees. The Board has committed the Management of the Company and its subsidiaries to be responsible for the day-to-day management and operation of the Group's businesses.

Composition of the Board

The Board consists of 8 Directors, including four executive Directors, namely Mr. Lam Kong, Mr. Chen Hongbing, Ms. Chen Yanling and Mr. Hui Ki Fat; one non-executive Director, namely Ms. Hou Xiaoxuan; and three independent non-executive Directors, namely Mr. Cheung Kam Shing, Terry, Dr. Peng Huaizheng and Mr. Wu Chi Keung. Biographical details of the Directors are set out on pages 19 to 21 of this annual report.

Board Attendances

During the reporting period, the Company held fifteen Board meetings. The following is the attendance record of Directors at Board meetings held during the reporting period.

Name	Title	Attendance Rate
Mr. Lam Kong	Chairman and CEO	14/15
Mr. Chen Hongbing	COO	14/15
Ms. Chen Yanling	CFO	15/15
Mr. Hui Ki Fat	Executive Director	14/15
Ms. Hou Xiaoxuan	Non-Executive Director	14/15
Dr. Peng Huaizheng*	Independent Non-Executive Director	6/15
Mr. Wu Chi Keung*	Independent Non-Executive Director	8/15
Mr. Cheung Kam Shing,Terry*	Independent Non-Executive Director	5/15
Dr. Paul Harper*	Independent Non-Executive Director	3/15
Mr. Stuart Leckie*	Independent Non-Executive Director	8/15

*Note: Dr. Peng Huaizheng, Mr. Wu Chi Keung and Mr. Cheung Kam Shing, Terry, were appointed as independent non-executive directors respectively on 4 May 2010, 25 June 2010 and 18 August 2010, Dr. Paul Harper and Mr. Stuart Leckie have resigned on 4 May 2010 and 2 August 2010 respectively.

Chairman and Chief Executive Officer

Rule A.2.1 of the Code stipulates that the roles of chairman of the board (the "Chairman") and Chief Executive Officer should be separate and should not be performed by the same individual. The division of responsibilities between the Chairman and chief executive officer should be clearly established and set out in writing.

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

Non-executive Directors

In full compliance with Rules 3.10(1) and (2) of the Listing Rules, from 28 September 2010 to 31 December 2010, the Company has appointed three Independent Non-executive Directors, at least one of whom has appropriate professional accounting qualifications. The Company has received from each Independent Non-executive Director an annual confirmation of his independence, and the Company considers such directors to be independent in accordance with each and every guideline set out under the Listing Rules.

The Non-executive Directors are appointed for a period of three years while Independent Non-executive Directors are appointed for a period of one year. All of them are subject to retirement by rotation and re-election by shareholders at AGM in accordance with the Articles of Association of the Company. The responsibilities of the Non-executive Directors include, without limitation: regular attendance at meetings of the Board and of Board Committees of which they are members; provision of independent opinions at meetings of the Board and other Board Committees; service on the Audit Committee, Remuneration Committee and Nomination Committee; and scrutinizing and monitoring the performance of the Company.

Committees

The Company has established Audit Committee, Remuneration Committee and Nomination Committee. The function of each specialized committee is to study pertinent issues in its area of expertise and to provide opinions and suggestions for consideration by the Board under defined terms of reference.

Audit Committee

We established an Audit Committee in 2007. The Audit Committee currently comprises three Independent Non-executive Directors, and is chaired by Mr. Wu Chi Keung, with Mr. Cheung Kam Shing,Terry and Dr. Peng Huaizheng as Committee members.

The primary duties of the Audit Committee are to provide our Directors with an independent review of the effectiveness of the financial reporting process, internal control and risk management system of our company, to oversee the audit process and to perform other duties and responsibilities as assigned by our Directors. The Audit Committee also oversee the company’s appointment of external auditors.The annual result announcement and annual report for the year ended 31 December 2010 have been reviewed by the Audit Committee, and with recommendation to the Board for approval.

For the year ended 31 December 2010, the Audit Committee has held three meetings on 21 January 2010, 30 March 2010, and 28 December 2010 respectively. Below is the attendance rate of the Committee members:

Mr.Wu Chi Keung (Chairman of Audit Committee), Mr. Cheung Kam Shing, Terry, and Dr. Peng Huaizheng, after being elected as members of the Audit Committee were present at the meeting on 28 December 2010, reviewed and approved the arrangement of the annual audit work and then proposed the suggestion to Board.

Committee Members	Attendance Rate of the Meeting for the Year ended 31 December 2010
Mr. Wu Chi Keung	1/3*
Mr. Cheung Kam Shing, Terry	1/3*
Dr. Peng Huaizheng	1/3*
Dr. Paul Harper	2/3*
Mr. Stuart Leckie	2/3*

*Notes: Mr.Wu Chi Keung, Mr. Cheung Kam Shing, Terry, and Dr. Peng Huaizheng were elected as the Audit Committee members in the board meeting which were respectively held on 4 June 2010, 2 August 2010, and 14 May 2010. The prior members of the Audit Committee Dr. Paul Harper and Mr. Stuart Leckie have resigned on 4 May 2010 and 2 August 2010 respectively.

Remuneration Committee

We established a remuneration committee in 2007. The remuneration committee comprises three Independent Non-executive Directors, and is chaired by Dr. Peng Huaizheng and comprises Mr. Cheung Kam Shing,Terry and Mr. Wu Chi Keung.

The primary duties of the Remuneration Committee include (but without limitation): (i) making recommendations to our Directors on our policy and structure for remunerations of all our Directors and senior management and on the establishment of a formal and transparent procedure for developing policies on such remuneration; (ii) determining the terms of the specific remuneration package of our Directors and senior management; and (iii) reviewing and approving performance-based remuneration by reference to corporate goals and objectives resolved by our Directors from time to time.

The Remuneration Committee held a meeting on 14 May 2010 the Chairman Dr. Peng Huaizheng and the prior Committee member Mr. Stuart Leckie were present at the meeting and approved the arrangement of remuneration for the Independent Non-executive Directors.

*Notes: The prior member of the remuneration committee Dr. Paul Harper and Mr. Stuart Leckie have resigned on 4 May 2010 and 2 August 2010 respectively.

Nomination Committee

We established the Nomination Committee in 2007. The Nomination Committee comprises one Executive Director and three Independent Non-executive Directors, and is chaired by Mr. Cheung Kam Shing, Terry and comprises Mr. Lam Kong, Dr. Peng Huaizheng and Mr. Wu Chi Keung.

The primary duties of the Nomination Committee are to make recommendations to our Directors on all new appointments of Directors and senior management, interviewing nominees, and to take up references and to consider related matters.

The Nomination Committee has held two meetings respectively on 30 March 2010 and 14 May 2010. The nomination and election of the relevant Committee members were discussed and approved in the meeting. Below is the attendance rate of the Committee members:

Committee Members	Attendance rate of the meeting for the year ended 31 December
Mr. Cheung Kam Shing, Terry	0/2*
Mr. Lam Kong	2/2
Mr. Wu Chi Keung	0/2*
Dr. Peng Huaizheng	0/2*
Dr. Paul Harper	1/2*
Mr. Stuart Leckie	2/2*

*Notes:Mr.Wu Chi Keung, Mr. Cheung Kam Shing, Terry and Dr. Peng Huaizheng were elected as the Nomination Committee members in the Board meeting which were respectively held on 4 June 2010, 2 August 2010, and 14 May 2010. The prior members of the Audit Committee Dr. Paul Harper and the chairman Mr. Stuart Leckie have resigned on 4 May 2010 and 2 August 2010 respectively.

Auditor's Remuneration

For the year ended 31 December 2010, we have appointed Deloitte Touche Tohmatsu as our independent external auditor to provide the annual performance auditing service, the remuneration for the service was HK$1.2 million.

Directors' and Auditor's Responsibilities for Accounts

The Board acknowledges their responsibility for presenting a balanced, clear and understandable assessment of annual and interim reports, price-sensitive announcements and other financial disclosures required under the Listing Rules and other regulatory requirements. The Directors confirm that they are responsible for the preparation of financial reports, and to give a true and fair view of the Company's and the Group's financial status and operating results for the year ended 31 December 2010 in preparing these financial statements, the Board has selected suitable accounting policies; made judgments and estimates that are prudent, fair and reasonable; and have prepared the consolidated financial statements on a going concern basis.

Internal Controls

The Directors are responsible for maintaining a reliable and effective internal control system. The Company has established an internal audit department with relatively independent internal audit functions. An audit committee and a risk management committee have also been established and are responsible to the Board. The Directors are in a position to supervise, assess and improve the Company's internal controls at all levels of management, so as to ensure that the Company can withstand changes in its operations and other external influences on its financial, operational and risk management, in order to safeguard the Company's assets and promote shareholders' interests.

During the reporting period, the Company further enhanced its internal control system, strengthened awareness on risk management, regulated work flows, promoted construction of ERP system and improved risk management; at the same time, the Company emphasized financial management and control functions of the Group, enhanced construction of financial system, strengthened audit function, stabilized investment procedures, and fully reinforced supervision efforts. Through series of measures, both internal management and operational efficiency of the Group have been significantly improved. The Board of Directors of the Company review its internal control system from time to time and consider that the internal control system of the Company is effective, resources in accounting and financial reporting functions, qualifications of staff and their experience are sufficient.

Communications with Investors

The Company places great emphasis on communication with investors. Since the successful listing of the Company in Hong Kong on 28 September 2010, the Company has established a dedicated department to handle affairs regarding investor relations and arrange for the site visit. The Company actively participated in various conferences and road shows organized by sell side agencies, and meet with many fund managers. The activities provide quality and effective information to investors and improve investors' understanding of the strategies and operation of the Company.

The Company has provided several effective communication channels, including direct interviews with investors or communication through telephone, email and letter. To allow investors understand the development of the Company, the investor relations department actively communicates with investors through sending the Company magazine and releasing Company's news.

The Company believes that shareholders' rights should be well respected and protected. From 28 September 2010 to 31 December 2010, the Company has disclosed all necessary information to the shareholders in compliance with the Listing Rules. We have reported to our shareholders and investors through various formal channels, and maintain good communications with shareholders and investors so that they may make an informed assessment for their investments and exercise their rights as shareholders. In the future, the Company will maintain effective communications with investors.

Deloitte.
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INDEPENDENT AUDITOR'S REPORT

TO THE MEMBERS OF
CHINA MEDICAL SYSTEM HOLDINGS LIMITED
康哲藥業控股有限公司
(FORMERLY KNOWN AS 康哲醫藥控股有限公司)
(incorporated in the Cayman Islands with limited liability)

We have audited the consolidated financial statements of China Medical System Holdings Limited (the "Company") and its subsidiaries (collectively referred to as the "Group") set out on pages 3 to 79, which comprise the consolidated statement of financial position as at 31 December 2010, and the consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information.

Directors' Responsibility for the Consolidated Financial Statements

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

Auditor's Responsibility

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

INDEPENDENT AUDITOR'S REPORT

TO THE MEMBERS OF
CHINA MEDICAL SYSTEM HOLDINGS LIMITED - continued
康哲藥業控股有限公司
(FORMERLY KNOWN AS 康哲醫藥控股有限公司)
(incorporated in the Cayman Islands with limited liability)

Auditor's Responsibility - continued

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

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

Opinion

In our opinion, the consolidated financial statements give a true and fair view of the state of affairs of the Group as at 31 December 2010, and of the Group's profit and cash flows for the year then ended in accordance with International Financial Reporting Standards and have been properly prepared in accordance with the disclosure requirements of the Hong Kong Companies Ordinance.

Deloitte Touche Tohmatsu
Certified Public Accountants
Hong Kong
24 February 2011

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME
FOR THE YEAR ENDED 31 DECEMBER 2010

	NOTES	2010 US$'000	2009 US$'000
Turnover	5	132,177	96,454
Cost of goods sold		(54,075)	(35,596)
Gross profit		78,102	60,858
Other gains and losses	6	373	662
Selling expenses		(30,966)	(24,840)
Listing expenses		(2,960)	-
Administrative expenses		(9,466)	(7,399)
Research and development costs		-	(2,038)
Finance costs	7	(617)	(390)
Share of results of associates		112	30
Share of result of a jointly controlled entity		56	43
Profit before taxation		34,634	26,926
Taxation	9	(3,943)	(6,096)
Profit for the year	10	30,691	20,830
Other comprehensive income			
Exchange differences from translation		1,782	70
Share of other comprehensive income of an associate		(5)	(1)
Fair value changes of qualifying hedging instruments for cash flow hedges		97	(145)
Total comprehensive income for the year		32,565	20,754
Profit for the year attributable to:			
Owners of the Company		30,587	20,684
Non-controlling interests		104	146
		30,691	20,830
Total comprehensive income attributable to:			
Owners of the Company		32,461	20,608
Non-controlling interests		104	146
		32,565	20,754

	NOTE	2010	2009
		US$ cent	US$ cent
Earnings per share	13		
Basic		3.061	2.186
Diluted		3.022	2.174

CONSOLIDATED STATEMENT OF FINANCIAL POSITION
AT 31 DECEMBER 2010

	NOTES	2010 US$'000	2009 US$'000
Non-current assets			
Property, plant and equipment	14	3,282	3,575
Prepaid lease payments	15	3,142	260
Interest in a jointly controlled entity	16	99	43
Interest in an associate	17	1,431	1,507
Intangible assets	18	5,368	6,461
Goodwill	19	379	379
Deferred tax assets	20	4,431	1,432
Deposit paid for acquisition of property, plant and equipment		478	-
		18,610	13,657
Current assets			
Inventories	21	15,978	11,060
Trade and other receivables	22	49,314	32,794
Amount due from a jointly controlled entity	23	673	481
Held for trading investments	24	38	31
Tax recoverable		77	-
Pledged bank deposits	25	4,530	17,641
Bank balances and cash	25	133,987	15,113
		204,597	77,120
Current liabilities			
Trade and other payables	26	8,252	11,062
Bank borrowings - secured	27	4,261	16,517
Deferred consideration payables	28	1,198	838
Derivative financial instruments	29	48	145
Tax payable		2,709	1,226
		16,468	29,788
Net current assets		188,129	47,332
Total assets less current liabilities		206,739	60,989

	NOTES	2010 US$'000	2009 US$'000
Capital and reserves			
Share capital	30	5,718	4,741
Reserves	32	194,271	48,992
Equity attributable to owners of the Company		199,989	53,733
Non-controlling interests		-	201
		199,989	53,934
Non-current liabilities			
Deferred tax liabilities	20	2,123	1,764
Deferred consideration payables	28	4,627	5,291
		6,750	7,055
		206,739	60,989

The consolidated financial statements on pages 39 to 115 were approved and authorised for issue by the Board of Directors on 24 February 2011 and are signed on its behalf by:

LAM Kong
DIRECTOR

CHEN Yanling
DIRECTOR

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY
FOR THE YEAR ENDED 31 DECEMBER 2010

	Attributable to the owners of the Company											
	Share capital US$'000	Share premium US$'000	Capital reserve US$'000 (note 32)	Share option reserve US$'000 (note 31)	Surplus reserve fund US$'000 (note 32)	Translation reserve US$'000	Hedging reserve US$'000	Accumulated profits US$'000	Dividend reserve US$'000	Total US$'000	Non-controlling interests US$'000	Total US$'000
Balance at 1 January 2009	4,725	17,147	4,911	570	6,057	5,661	-	8,994	4,725	52,790	(69)	52,721
Exchange differences arising from translation	-	-	-	-	-	70	-	-	-	70	-	70
Share of other comprehensive income of an associate	-	-	-	-	-	(1)	-	-	-	(1)	-	(1)
Fair value changes of qualifying hedging instruments for cash flow hedges	-	-	-	-	-	-	(145)	-	-	(145)	-	(145)
Profit for the year	-	-	-	-	-	-	-	20,684	-	20,684	146	20,830
Total comprehensive income and expense for the year	-	-	-	-	-	69	(145)	20,684	-	20,608	146	20,754
Issue of shares	16	435	-	-	-	-	-	-	-	451	-	451
Release of translation reserve upon disposal of subsidiary	-	-	-	-	-	8	-	(8)	-	-	-	-
Release of translation reserve upon disposal of an associate	-	-	-	-	-	(36)	-	36	-	-	-	-
Dividends paid to a non-controlling shareholder	-	-	-	-	-	-	-	-	-	-	(206)	(206)
Effect of distribution in specie	-	(11,503)	-	-	-	853	-	-	-	(10,650)	330	(10,320)
Dividends paid	-	-	-	-	-	-	-	(4,741)	(4,725)	(9,466)	-	(9,466)
Dividends proposed - 2009	-	-	-	-	-	-	-	(4,741)	4,741	-	-	-
Transfer of reserves	-	-	-	-	2,102	-	-	(2,102)	-	-	-	-
Balance at 31 December 2009	4,741	6,079	4,911	570	8,159	6,555	(145)	18,122	4,741	53,733	201	53,934

	Share capital US$'000	Share premium US$'000	Capital reserve US$'000 (note 32)	Share option reserve US$'000 (note 31)	Surplus reserve fund US$'000 (note 32)	Translation reserve US$'000	Hedging reserve US$'000	Accumulated profits US$'000	Dividend reserve US$'000	Total US$'000	Non-controlling interests US$'000	Total US$'000
	Attributable to the owners of the Company											
Exchange differences arising from translation	-	-	-	-	-	1,782	-	-	-	1,782	-	1,782
Share of other comprehensive income of an associate	-	-	-	-	-	(5)	-	-	-	(5)	-	(5)
Fair value changes of qualifying hedging instruments for cash flow hedges	-	-	-	-	-	-	97	-	-	97	-	97
Profit for the year	-	-	-	-	-	-	-	30,587	-	30,587	104	30,691
Total comprehensive income for the year	-	-	-	-	-	1,777	97	30,587	-	32,461	104	32,565
Issue of shares	1	103	-	-	-	-	-	-	-	104	-	104
Issue of shares in consideration of acquisition of additional interest in a subsidiary	26	2,299	-	-	-	-	-	-	-	2,325	-	2,325
Issue of new shares for cash (note 30)	850	110,030	-	-	-	-	-	-	-	110,880	-	110,880
Issue of new shares for cash under over-allotment option (note 30)	100	12,945	-	-	-	-	-	-	-	13,045	-	13,045
Issue costs of new shares	-	(4,965)	-	-	-	-	-	-	-	(4,965)	-	(4,965)
Deemed distribution to a shareholder	-	-	(632)	-	-	-	-	-	-	(632)	-	(632)
Acquisition of additional interest in a subsidiary	-	-	(2,221)	-	-	-	-	-	-	(2,221)	(104)	(2,325)
Dividends paid to a non-controlling shareholder	-	-	-	-	-	-	-	-	-	-	(201)	(201)
Dividends paid	-	-	-	-	-	-	-	-	(4,741)	(4,741)	-	(4,741)
Dividends proposed - 2010	-	-	-	-	-	-	-	(14,868)	14,868	-	-	-
Transfer of reserves	-	-	-	-	999	-	-	(999)	-	-	-	-
Balance at 31 December 2010	5,718	126,491	2,058	570	9,158	8,332	(48)	32,842	14,868	199,989	-	199,989

CONSOLIDATED STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED 31 DECEMBER 2010

	NOTES	2010 US$'000	2009 US$'000
Operating activities			
Profit before taxation		34,634	26,926
Adjustments for:			
Share of results of associates		(112)	(30)
Share of result of a jointly controlled entity		(56)	(43)
Discount on acquisition of an associate		-	(647)
Amortisation of intangible assets	18	839	1,115
Depreciation of property, plant and equipment	14	724	898
Release of prepaid lease payments		67	7
Interest income		(505)	(329)
Interest expenses		327	43
Imputed interest expense on deferred consideration payables		290	347
Listing expenses		2,960	-
Gain on disposal of property, plant and equipment		(1)	(7)
Impairment loss recognised on property, plant and equipment		-	805
Gain on disposal of a subsidiary		-	(24)
Loss on disposal of an associate		-	70
Allowance for inventories		222	10
Allowance for bad and doubtful debts		18	57
Operating cash flows before movements in working capital		39,407	29,198
Increase in inventories		(4,797)	(5,226)
Increase in trade and other receivables		(15,224)	(5,287)
Increase in held for trading investments		(7)	(31)
Decrease in amount due from an associate		-	172
Increase in amount due from a jointly controlled entity		(192)	(481)
Increase in amounts due from directors		-	43
(Decrease) increase in trade and other payables		(2,802)	2,284
Cash generated from operations		16,385	20,672
PRC Enterprise Income Tax paid		(5,068)	(5,008)
Hong Kong Profits Tax paid		(126)	(115)
Net cash from operating activities		11,191	15,549

	NOTE	2010 US$'000	2009 US$'000
Investing activities			
Purchase of property, plant and equipment		(832)	(280)
Purchase of land use right		(2,918)	-
Decrease (increase) in pledged bank deposits		13,111	(16,581)
Interest received		505	329
Dividend received from an associate		183	235
Proceeds from disposal of property, plant and equipment		27	120
Cash outflow from disposal of a subsidiary		-	(1)
Proceeds from disposal of an associate		-	439
Acquisition of an associate		-	(877)
Net cash from (used in) investing activities		10,076	(16,616)
Financing activities			
Interest paid		(370)	-
Dividends paid		(4,741)	(9,471)
Cash outflow from distribution in specie	35(a)	-	(10,068)
Repayment of deferred consideration payables		(774)	(1,245)
Proceeds from issue of shares		124,029	451
New bank borrowings raised		4,261	16,517
Expenses incurred in connection with listing of shares to Main Board		(8,557)	-
Repayment of borrowings		(16,517)	-
Dividends paid to a non-controlling shareholder		(201)	(206)
Net cash from (used in) financing activities		97,130	(4,022)
Net increase (decrease) in cash and cash equivalents		118,397	(5,089)
Cash and cash equivalent at beginning of the year		15,113	20,100
Effect of foreign exchange rate changes		477	102
Cash and cash equivalent at end of the year, represented by bank balances and cash		133,987	15,113

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2010

1. GENERAL

The Company was incorporated as an exempted company with limited liability in the Cayman Islands on 18 December 2006. On 26 June 2007, the Company was listed on the Alternative Investment Market ("AIM") operated by the London Stock Exchange plc. The Company was listed on the Main Board operated by the Stock Exchange of Hong Kong Limited on 28 September 2010 and it was delisted from the AIM on the same date. The Company's ultimate holding company and immediate holding company is Treasure Sea Limited, a company incorporated in the British Virgin Islands. The address of the Company's registered office is P.O. Box 309, Ugland House, Grand Cayman, KY1-1104, Cayman Islands. The address of its principal place of business is 8/F., Block A, Tong Fong Information Centre, Long Shan Road, Nan Shan, Shenzhen, the People's Republic of China (the "PRC").

The Company is a investment holding company. The principal activities of its subsidiaries are production of medicines, distribution and import of drugs.

The functional currency of the Company is Renminbi as it is the currency in which the majority of the Group's transactions are denominated. The consolidated financial statements of the Group are presented in United States Dollars ("US$"), which is a currency widely and commonly recognised in the global economy and is freely convertible into a number of foreign currencies. Therefore, the directors consider the presentation in US$ to be more useful for its current and potential investors.

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

In the current year, the Group has applied the following new and revised standards or interpretations (hereinafter collectively referred to as "new and revised IFRSs") issued by the International Accounting Standards Board (the "IASB") and IFRS Interpretations Committee (formerly known as the International Financial Reporting Interpretation Committee) (the "IFRIC") of the IASB that are effective for the Group's financial year beginning on 1 January 2010.

IFRS 2 (Amendments)	Group cash-settled share-based payment transactions
IFRS 3 (as revised in 2008)	Business combinations
IAS 27 (as revised in 2008)	Consolidated and separate financial statements
IAS 39 (Amendments)	Eligible hedged items
IFRSs (Amendments)	Improvements to IFRSs issued in 2009
IFRSs (Amendments)	Amendments to IFRS 5 as part of improvements to IFRSs issued in 2008
IFRIC - INT 17	Distributions of non-cash assets to owners

Except as disclosed below, the adoption of the new and revised IFRSs has had no material effect on the consolidated financial statements of the Group for the current or prior accounting periods.

IAS 27 (as revised in 2008) Consolidated and Separate Financial Statements

The application of IAS 27(as revised in 2008) has resulted in changes in the Group's accounting policies for changes in ownership interests in subsidiaries of the Group.

Specifically, the revised Standard has affected the Group's accounting policies regarding changes in the Group's ownership interests in its subsidiaries that do not result in loss of control. In prior years, in the absence of specific requirements in IFRSs, increases in interests in existing subsidiaries were treated in the same manner as the acquisition of subsidiaries, with goodwill or a bargain purchase gain being recognised, when appropriate; for decreases in interests in existing subsidiaries that did not involve a loss of control, the difference between the consideration received and the adjustment to the non-controlling interests was recognised in profit or loss. Under IAS 27(as revised in 2008), all such increases or decreases are dealt with in equity, with no impact on goodwill or profit or loss.

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

IAS 27 (as revised in 2008) Consolidated and Separate Financial Statements - continued

When control of a subsidiary is lost as a result of a transaction, event or other circumstance, the revised Standard requires the Group to derecognise all assets, liabilities and non-controlling interests at their carrying amounts and to recognise the fair value of the consideration received. Any retained interest in the former subsidiary is recognised at its fair value at the date control is lost. The resulting difference is recognised as a gain or loss in profit or loss.

These changes have been applied prospectively from 1 January 2010 in accordance with the relevant transitional provisions.

The application of the revised Standard has affected the accounting for the Group's acquisition of additional interest in a subsidiary, Sky United Trading Limited ("Sky United"), in the current year. The change in policy has resulted in the recognition of the excess of consideration payable over the decrease in the carrying value of the non-controlling interest amounting to US$2,221,000 in equity (capital reserve).

The Group has not early applied the following new and revised Standards and Interpretations that have been issued but are not yet effective:

IFRSs (Amendments)	Improvements to IFRSs issued in 2010 except for the amendments to IFRS 3 (as revised in 2008), IAS 1 and IAS 28[1]
IFRS 7 (Amendments)	Disclosures - Transfers of financial assets[3]
IFRS 9	Financial instruments[4]
IAS 12 (Amendments)	Deferred tax: Recovery of underlying assets[5]
IAS 24 (as revised in 2009)	Related party disclosures[6]
IAS 32 (Amendments)	Classification of rights issues[7]
IFRIC - INT 14 (Amendments)	Prepayments of a minimum funding requirement[6]
IFRIC - INT 19	Extinguishing financial liabilities with equity instruments[2]

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

[1] Effective for annual periods beginning on or after 1 July 2010 or 1 January 2011, as appropriate.
[2] Effective for annual periods beginning on or after 1 July 2010.
[3] Effective for annual periods beginning on or after 1 January 2011.
[4] Effective for annual periods beginning on or after 1 January 2013.
[5] Effective for annual periods beginning on or after 1 January 2012.
[6] Effective for annual periods beginning on or after 1 January 2011.
[7] Effective for annual periods beginning on or after 1 February 2010.

IFRS 9 "Financial instruments" (as issued in November 2009) introduces new requirements for the classification and measurement of financial assets. IFRS 9 "Financial instruments" (as revised in November 2010) adds requirements for financial liabilities and for derecognition. Specifically, under IFRS 9, all recognised financial assets that are within the scope of IAS 39 "Financial instruments: recognition and measurement" are subsequently measured at either amortised cost or fair value. Specifically, debt investments that are held within a business model whose objective is to collect the contractual cash flows, and that have contractual cash flows that are solely payments of principal and interest on the principal outstanding are generally measured at amortised cost at the end of subsequent accounting periods. All other debt investments and equity investments are measured at their fair values at the end of subsequent accounting periods.

IFRS 9 is effective for annual periods beginning on or after 1 January 2013, with earlier application permitted. The directors anticipate that the application of IFRS 9 will have no significant impact on amounts reported in respect of the Groups' financial assets and financial liabilities.

The directors of the Company anticipate that the application of the other new and revised standards or interpretations will have no material impact on the Group's results and the financial position of the Group.

3. SIGNIFICANT ACCOUNTING POLICIES

The consolidated financial statements have been prepared in accordance with the following accounting policies which conform with IFRSs. In addition, the consolidated financial statements include applicable disclosures required by the Rules Governing the Listing of Securities on the Stock Exchange and by the Hong Kong Companies Ordinance.

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

Basis of consolidation

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

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

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

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

Non-controlling interests in subsidiaries are presented separately from the Group's equity therein.

Allocation of total comprehensive income to non-controlling interests

Total comprehensive income and expense of a subsidiary is attributed to the owners of the Company and to the non-controlling interests even if this results in the non-controlling interests having a deficit balance. Prior to 1 January 2010, losses applicable to the non-controlling interests in excess of the non-controlling interests in the subsidiary's equity were not allocated against the interests of the Group except to the extent that the non-controlling interests had a binding obligation and were able to make an additional investment to cover the losses.

3. SIGNIFICANT ACCOUNTING POLICIES - continued

Changes in the Group's ownership interests in existing subsidiaries

Changes in the Group's ownership interests in existing subsidiaries on or after 1 January 2010

Changes in the Group's ownership interest in a subsidiary that do not result in the Group losing control over the subsidiary are accounted for as equity transactions. The carrying amounts of the Group's interests and the non-controlling interests are adjusted to reflect the changes in their relative interests in the subsidiaries. Any difference between the amount by which the non-controlling interests are adjusted and the fair value of the consideration paid or received is recognised directly in equity and attributed to owners of the Company. Where the consideration for the acquisition of the additional interest in a subsidiary is in the form of ordinary shares of the Company, the consideration is determined by reference to the fair value of the shares at date of acquisition.

Increases in interests in existing subsidiaries were treated in the same manner as the acquisition of subsidiaries, with goodwill or a bargain purchase gain being recognised where appropriate. For decreases in interests in subsidiaries regardless of whether the disposals would result in the Group losing control over the subsidiaries, the difference between the consideration received and the carrying amount of the share of net assets disposed of was recognised in profit or loss.

Business combinations

Business combinations on or after 1 January 2010

Acquisitions of businesses are accounted for using the acquisition method. The consideration transferred in a business combination is measured at fair value, which is calculated as the sum of the acquisition-date fair values of the assets transferred by the Group, liabilities incurred by the Group to former owners of the acquiree and the equity interests issued by the Group in exchange for control of the acquiree. Acquisition-related costs are generally recognised in profit or loss as incurred.

3. SIGNIFICANT ACCOUNTING POLICIES - continued

Business combinations - continued

Business combinations on or after 1 January 2010 - continued

At the acquisition date, the identifiable assets acquired and the liabilities assumed are recognised at their fair values at the acquisition date, except that:

- deferred tax assets or liabilities and liabilities or assets related to employee benefit arrangements are recognised and measured in accordance with IAS 12 "Income taxes" and IAS 19 "Employee benefits" respectively;

- liabilities or equity instruments related to share-base payment transactions of the acquiree or the replacement of an acquiree's share-based payment transactions are measured in accordance with IFRS 2 "Share-based payment" at the acquisition date; and

- assets (or disposal groups) that are classified as held for sale in accordance with IFRS 5 "Non-current assets held for sale and discontinued operations" are measured in accordance with that Standard.

Goodwill is measured as the excess of the sum of the consideration transferred, the amount of any non-controlling interests in the acquiree, and the fair value of the acquirer's previously held equity interest in the acquiree (if any) over the net of the acquisition-date amounts of the identifiable assets acquired and the liabilities assumed. If, after re-assessment, the net of the acquisition-date amounts of the identifiable assets acquired and liabilities assumed exceeds the sum of the consideration transferred, the amount of any non-controlling interests in the acquiree and the fair value of the acquirer's previously held interest in the acquiree (if any), the excess is recognised immediately in profit or loss as a bargain purchase gain.

Non-controlling interests that are present ownership interests and entitle their holders to a proportionate share of the entity's net assets in the event of liquidation may be initially measured either at fair value or at the non-controlling interests' proportionate share of the recognised amounts of the acquiree's identifiable net assets. The choice of measurement basis is made on a transaction-by-transaction basis. Other types of non-controlling interests are measured at their fair value or another measurement basis required by another Standard.

3. SIGNIFICANT ACCOUNTING POLICIES - continued

Business combinations - continued

Business combinations prior to 1 January 2010

Acquisition of businesses was accounted for using the purchase method. The cost of the acquisition was measured at the aggregate of the fair values, at the date of exchange, of assets given, liabilities incurred or assumed, and equity instruments issued by the Group in exchange for control of the acquiree, plus any costs directly attributable to the business combination. The acquiree's identifiable assets, liabilities and contingent liabilities that met the relevant conditions for recognition were generally recognised at their fair values at the acquisition date.

Goodwill arising on acquisition was recognised as an asset and initially measured at cost, being the excess of the cost of the business combination over the Group's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities recognised. If, after assessment, the Group's interest in the net fair value of the acquiree's identifiable assets, liabilities and contingent liabilities exceeded the cost of the business combination, the excess was recognised immediately in profit or loss.

The non-controlling interest in the acquiree was initially measured at the non-controlling interest's proportionate share of the net fair value of the assets, liabilities and contingent liabilities of the acquiree.

Distribution in specie

The amount recognised as distribution in respect of a distribution in specie is measured at the carrying value of assets and liabilities of the subsidiaries being distributed at the date of the distribution.

3. SIGNIFICANT ACCOUNTING POLICIES - continued

Goodwill

Goodwill arising on an acquisition of a business is carried at cost less any accumulated impairment losses, if any, and is presented separately in the consolidated statement of financial position.

A cash-generating unit to which goodwill has been allocated is tested for impairment annually, or more frequently whenever there is indication that the unit may be impaired. For goodwill arising on an acquisition in a reporting period, the cash-generating unit to which goodwill has been allocated is tested for impairment before the end of that reporting period. If the recoverable amount of the cash-generating unit is less than the carrying amount of the unit, the impairment loss is allocated first to reduce the carrying amount of any goodwill allocated to the unit and then to the other assets of the unit pro rata on the basis of the carrying amount of each asset in the unit. Any impairment loss for goodwill is recognised directly in profit or loss in the consolidated statement of comprehensive income. An impairment loss recognised for goodwill is not reversed in subsequent periods.

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

Investment in an associate

An associate is an entity over which the investor has significant influence and that is neither a subsidiary nor an interest in a joint venture. Significant influence is the power to participate in the financial and operating policy decisions of the investee but is not control or joint control over those policies.

The results and assets and liabilities of associates are incorporated in these consolidated financial statements using the equity method of accounting. Under the equity method, investments in associates are carried in the consolidated statement of financial position at cost as adjusted for post-acquisition changes in the Group's share of the net assets of the associate, less any identified impairment loss. When the Group's share of losses of an associate equals or exceeds its interest in that associate (which includes any long-term interests that, in substance, form part of the Group's net investment in the associate), the Group discontinues recognising its share of further losses. Additional losses are recognised only to the extent that the Group has incurred legal or constructive obligations or made payments on behalf of that associate.

3. SIGNIFICANT ACCOUNTING POLICIES - continued

Investment in an associate - continued

Any excess of the Group's share of the net fair value of the identifiable assets, liabilities and contingent liabilities over the cost of acquisition, after reassessment, is recognised immediately in profit or loss.

When a group entity transacts with its associate, profits and losses resulting from the transactions with the associate are recognised in the Group' consolidated financial statements only to the extent of interests in the associate that are not related to the Group.

Investment in a jointly controlled entity

Joint venture arrangements that involve the establishment of a separate entity in which venturers have joint control over the economic activity of the entity are referred to as a jointly controlled entity.

The results and assets and liabilities of a jointly controlled entity are incorporated in the consolidated financial statements using the equity method of accounting. Under the equity method, investment in a jointly controlled entity is carried in the consolidated statement of financial position at cost as adjusted for post-acquisition changes in the Group's share of the net assets of the jointly controlled entity, less any identified impairment loss. When the Group's share of losses of a jointly controlled entity equals or exceeds its interest in that jointly controlled entity (which includes any long-term interests that, in substance, form part of the Group's net investment in the jointly controlled entity), the Group discontinues recognising its share of further losses. Additional losses are recognised only to the extent that the Group has incurred legal or constructive obligations or made payments on behalf of that jointly controlled entity.

When a group entity transacts with its jointly controlled entity, profits and losses resulting from the transactions with the jointly controlled entity are recognised in the Group' consolidated financial statements only to the extent of interests in the jointly controlled entity that are not related to the Group.

3. SIGNIFICANT ACCOUNTING POLICIES - continued

Intangible assets

Intangible assets acquired separately with finite useful lives are carried at cost less accumulated amortisation and any accumulated impairment losses. Amortisation for intangible assets with finite useful lives is provided on a straight line basis over their estimated useful lives.

Gains or losses arising from derecognition of an intangible asset are measured as the difference between the net disposal proceeds and the carrying amount of the asset and are recognised in profit or loss in the period when the asset is derecognised.

Research and development expenditure

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

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

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

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

3. SIGNIFICANT ACCOUNTING POLICIES - continued

Revenue recognition

Revenue is measured at the fair value of the consideration received or receivable and represents amounts receivable for good sold in the normal course of business, net of customer returns, rebates, other similar allowances and sales related taxes.

Revenue from the sale of goods is recognised when goods are delivered and title has passed.

Service fee income is recognised as services are rendered.

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

Property, plant and equipment

Property, plant and equipment including buildings held for use in the production or supply of goods or services, or for administrative purposes are stated at cost less subsequent accumulated depreciation and accumulated impairment losses.

Depreciation is recognised so as to write off the cost of items of property, plant and equipment less their residual values over their estimated useful lives, using the straight-line method. The estimated useful lives, residual values and depreciation method are reviewed at the end of each reporting period, with the effect of any changes in estimate accounted for on a prospective basis.

Properties in the course of construction for production, supply or administrative purposes are carried at cost, less any recognised impairment loss. Costs include professional fees and, for qualifying assets, borrowing costs capitalised in accordance with the Group's accounting policy. Such properties are classified to the appropriate categories of property, plant and equipment when completed and ready for intended use. Depreciation of these assets, on the same basis as other property assets, commences when the assets are ready for their intended use.

An item of property, plant and equipment is derecognised upon disposal or when no future economic benefits are expected to arise from the continued use of the asset. Any gain or loss arising on the disposal or retirement of an item of property, plant and equipment is determined as the difference between the sales proceeds and the carrying amount of the asset and is recognised in profit or loss.

3. SIGNIFICANT ACCOUNTING POLICIES - continued

Impairment losses on tangible and intangible assets other than goodwill

At the end of each reporting period, the Group reviews the carrying amounts of its tangible and intangible assets to determine whether there is any indication that those assets have suffered an impairment loss. If the recoverable amount of an asset is estimated to be less than its carrying amount, the carrying amount of the asset is reduced to its recoverable amount. An impairment loss is recognised as an expense immediately.

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

Prepaid lease payments

Prepaid lease payments represent the cost of land use rights paid to the local Land Bureau of the PRC Government.

Land use rights are stated at cost and are charged to profit or loss in the consolidated statement of comprehensive income over the period for which the relevant land use right has been granted to the Group.

Inventories

Inventories are stated at the lower of cost and net realisable value. Cost is calculated using the weighted average method.

Financial instruments

Financial assets and financial liabilities are recognised in the consolidated statements of financial position when a group entity becomes a party to the contractual provisions of the instrument.

Financial assets and financial liabilities are initially measured at fair value. Transaction costs that are directly attributable to the acquisition or issue of financial assets and financial liabilities (other than financial assets or financial liabilities at fair value through profit or loss) are added to or deducted from the fair value of the financial assets or financial liabilities, as appropriate, on initial recognition. Transaction costs directly attributable to the acquisition of financial assets or financial liabilities at fair value through profit or loss are recognised immediately in profit or loss.

3. SIGNIFICANT ACCOUNTING POLICIES - continued

Financial instruments - continued

Financial assets

The Group's financial assets are classified into financial assets held for trading and loans and receivables. All regular way purchases or sales of financial assets are recognised and derecognised on a trade date basis. Regular way purchases or sales are purchases or sales of financial assets that require delivery of assets within the time frame established by regulation or convention in the marketplace. The accounting policies adopted in respect of each category of financial assets are set out below.

Effective interest method

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

Interest income is recognised on an effective interest basis for debt instruments.

Financial assets held for trading

A financial asset is classified as held for trading if:

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

At the end of the reporting period subsequent to initial recognition, financial assets held for trading are measured at fair value, with changes in fair value recognised directly in profit or loss in the period in which they arise. The net gain or loss recognised in profit or loss excludes any dividend or interest earned on the financial assets and are recognised in the "other gains and losses" line item (note 6) in the consolidated statement of comprehensive income.

3. SIGNIFICANT ACCOUNTING POLICIES - continued

Financial instruments - continued

Financial assets - continued

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Subsequent to initial recognition, loans and receivables (including trade and other receivables, amount due from a jointly controlled entity, pledged bank deposits, bank balances and cash) are carried at amortised cost using the effective interest method, less any identified impairment losses (see accounting policy on impairment loss on financial assets below).

Impairment of financial assets

Financial assets, other than financial assets held for trading, are assessed for indicators of impairment at the end of the reporting period. Financial assets are impaired where there is objective evidence that, as a result of one or more events that occurred after the initial recognition of the financial asset, the estimated future cash flows of the financial assets have been affected.

Objective evidence of impairment could include:

- significant financial difficulty of the issuer or counterparty; or
- breach of contract, such as default or delinquency in interest or principal payments; or
- it becoming probable that the borrower will enter bankruptcy or financial re-organisation.

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

For financial assets carried at amortised cost, an impairment loss is recognised in profit or loss when there is objective evidence that the asset is impaired, and is measured as the difference between the asset's carrying amount and the present value of the estimated future cash flows discounted at the original effective interest rate.

3. SIGNIFICANT ACCOUNTING POLICIES - continued

Financial instruments - continued

Impairment of financial assets - continued

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

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

Financial liabilities and equity

Financial liabilities and equity instruments issued by a group entity are classified according to the substance of the contractual arrangements entered into and the definitions of a financial liability and an equity instrument. An equity instrument is any contract that evidences a residual interest in the assets of the Group after deducting all of its liabilities.

Effective interest method

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

Interest expense is recognised on an effective interest basis for debt instruments.

Financial liabilities

The Group's financial liabilities, including trade and other payables, bank borrowings and deferred consideration payables, are subsequently measured at amortised cost, using the effective interest method.

3. SIGNIFICANT ACCOUNTING POLICIES - continued

Financial instruments - continued

Equity instruments

Equity instruments issued by the Company are recorded at the proceeds received, net of direct issue costs.

Derivative financial instruments and hedging

Derivatives are initially recognised at fair value at the date derivative contracts are entered into and are subsequently remeasured to their fair values at the end of the reporting period. The resulting gain or loss is recognised in profit or loss immediately unless the derivative is designated and effective as a hedging instrument, in which event the timing of the recognition in profit or loss depends on the nature of the hedge relationship.

Hedge accounting

The Group uses derivative financial instruments (primarily interest rate swaps and foreign currency forward contracts) to hedge its exposure against changes in interest rate and foreign currency exposure on bank borrowings. At the inception of the hedging relationship the entity documents the relationship between the hedging instrument and hedged item, along with its risk management objectives and its strategy for undertaking various hedge transactions. Furthermore, at the inception of the hedge and on an ongoing basis, the Group documents whether the hedging instrument that is used in a hedging relationship is highly effective in offsetting changes in cash flows of the hedged item.

Cash flow hedge

The effective portion of changes in the fair value of derivatives that are designated as qualifying hedging instruments for cash flow hedges are recognised in other comprehensive income. The gain or loss relating to the ineffective portion, if any, is recognised immediately in profit or loss as other gains or losses.

Amounts previously recognised in other comprehensive income and accumulated in equity (hedging reserve) are reclassified to profit or loss in the periods when the hedged item is recognised in profit or loss.

Hedge accounting is discontinued when the Group revokes the hedging relationship, the hedging instrument expires or is sold, terminated, or exercised, or no longer qualifies for hedge accounting.

3. SIGNIFICANT ACCOUNTING POLICIES - continued

Financial instruments - continued

Derecognition

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

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

Taxation

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

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

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

3. SIGNIFICANT ACCOUNTING POLICIES - continued

Taxation - continued

Deferred tax liabilities are recognised for taxable temporary differences associated with investments in subsidiaries and an associate, and interest in a jointly controlled entity, except where the Group is able to control the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future. Deferred tax assets arising from deductible temporary differences associated with such investments and interests are only recognised to the extent that it is probable that there will be sufficient taxable profits against which to utilise the benefits of the temporary differences and they are expected to reverse in the foreseeable future.

The carrying amount of deferred tax assets are reviewed at the end of the reporting period and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the assets to be recovered.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply in the period in which the liability is settled or the asset is realised, based on tax rate (and tax laws) that have been enacted or substantively enacted by the end of the reporting period. The measurement of deferred tax liabilities and assets reflects the tax consequences that would follow from the manner in which the Group expects, at the end of the reporting period, to recover or settle the carrying amount of its assets and liabilities. Deferred tax is recognised in profit or loss, except when it relates to items that are recognised in other comprehensive income or directly in equity, in which case the deferred tax is also recognised in other comprehensive income or directly in equity respectively.

Foreign currencies

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

Exchange differences arising on the settlement of monetary items, and on the translation of monetary items, are recognised in profit or loss in the period in which they arise.

3. SIGNIFICANT ACCOUNTING POLICIES - continued

Foreign currencies - continued

For the purposes of presenting the consolidated financial statements, the assets and liabilities of the Group's operations are translated from the functional currency of the respective companies into the presentation currency of the Group (i.e. US$) at the rate of exchange prevailing at the end of the reporting period, and their income and expenses are translated at the average exchange rates for the year, unless exchange rates fluctuate significantly during the period, in which case, the exchange rates prevailing at the dates of transactions are used. Exchange differences arising, if any, are recognised in other comprehensive income and accumulated in equity (the translation reserve).

From 1 January 2010 onwards, on the disposal of a foreign operation (i.e. a disposal of the Group's entire interest in a foreign operation, or a disposal involving loss of control over a subsidiary that includes a foreign operation, a disposal involving loss of joint control over a jointly controlled entity that includes a foreign operation, or a disposal involving loss of significant influence over an associate that includes a foreign operation), all of the exchange differences accumulated in equity in respect of that operation attributable to the owners of the Company are reclassified to profit or loss. In addition, in relation to a partial disposal of a subsidiary that does not result in the Group losing control over the subsidiary, the proportionate share of accumulated exchange differences are re-attributed to non-controlling interests and are not recognised in profit or loss. For all other partial disposals (i.e. partial disposals of associates or jointly controlled entities that do not result in the Group losing significant influence or joint control), the proportionate share of the accumulated exchange differences is reclassified to profit or loss.

Leasing

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

The Group as lessee

Operating lease payments are recognised as an expense on a straight-line basis over the lease term, except where another systematic basis is more representative of the time pattern in which economic benefits from the leased asset are consumed. Contingent rentals arising under operating leases are recognised as an expense in the period in which they are incurred.

In the event that lease incentives are received to enter into operating leases, such incentives are recognised as a liability. The aggregate benefit of incentives is recognised as a reduction of rental expense on a straight-line basis, except where another systematic basis is more representative of the time pattern in which economic benefits from the leased asset are consumed.

3. SIGNIFICANT ACCOUNTING POLICIES - continued

Leasehold land and building

When a lease includes both land and building elements, the Group assesses the classification of each element as a finance or an operating lease separately based on the assessment as to whether substantially all the risks and rewards incidental to ownership of each element have been transferred to the Group. Specifically, the minimum lease payments (including any lump-sum upfront payments) are allocated between the land and the building elements in proportion to the relative fair values of the leasehold interests in the land element and building element of the lease at the inception of the lease.

To the extent the allocation of the lease payments can be made reliably, interest in leasehold land that is accounted for as an operating lease is presented as "prepaid lease payments" in the consolidated statement of financial position and is amortised over the lease term on a straight-line basis. When the lease payments cannot be allocated reliably between the land and building elements, the entire lease is generally classified as a finance lease and accounted for as property, plant and equipment, unless it is clear that both elements are operating leases, in which case the entire lease is classified as an operating lease.

Borrowing costs

Borrowing costs directly attributable to the acquisition, construction or production of qualifying assets, which are assets that necessarily take a substantial period of time to get ready for their intended use or sale, are added to the cost of those assets until such time as the assets are substantially ready for their intended use or sale. Investment income earned on the temporary investment of specific borrowings pending their expenditure on qualifying assets is deducted from the borrowing costs eligible for capitalisation.

Government grants

Government grants are recognised in profit or loss on a systematic basis over the periods in which the Group recognises as expenses the related costs for which the grants are intended to compensate. Specifically, government grants whose primary condition is that the Group should purchase, construct or otherwise acquire non-current assets are recognised as a deduction from the carrying amount of the relevant asset in the consolidated statement of financial position and transferred to profit or loss over the useful lives of the related assets. Government grants that are receivable as compensation for expenses or losses already incurred or for the purpose of giving immediate financial support to the Group with no future related costs are recognised in profit or loss in the period in which they become receivable.

3. SIGNIFICANT ACCOUNTING POLICIES - continued

Retirement benefit costs

Payments to state-managed retirement benefit schemes, which are defined contribution schemes, are charged as an expense when employees have rendered service entitling them to the contributions.

Equity-settled share-based payment transactions

Share options granted to employees

A shareholder of the Company has granted shares to certain employees of the Group, for their services rendered for nil consideration. The fair value of services received is determined by reference to the fair value of the shares granted determined at the respective grant dates because the fair value of services cannot be reliably measured. Such fair value is recognised as an expense in full at the grant date with a corresponding increase in capital reserve.

Share options granted to the underwriter

Share options issued in exchange for services in connection with the underwriting of the new shares of the Company by way of placing and public offer are measured at the fair values of the services received, unless that fair value cannot be reliably measured, in which case the services received are measured by reference to the fair value of the share options granted. The fair values of the services received in relation to issue of new shares are recognised in other comprehensive income (share options reserve).

At the time when the share options are exercised, the amount previously recognised in share options reserve will be transferred to share premium. When the share options are forfeited after the vesting date or are still not exercised at the expiry date, the amount previously recognised in share options reserve will be transferred to share premium.

4. KEY SOURCES OF ESTIMATION UNCERTAINTY

The key assumptions concerning the future, and other key sources of estimation uncertainty at the end of the reporting period, that have a significant risk of causing a material adjustment to the carrying amount of assets and liabilities, are described below.

Impairment of intangible assets

The impairment of the intangible assets is based on the valuation of the recoverable amount with reference to the expected future cash flows estimated by management. Judgement is required in estimating the expected future cash flows from the Group's distribution right and agency right in connection to two finished drug products under the trade name of Nesiritide and Augentropfen Stulln Mono respectively. If the actual future cash flows are less than expected, impairment may be required. The carrying amount of the intangible assets as at 31 December 2010 is US$5,368,000 (2009: US$6,461,000) (see note 18).

Impairment of property, plant and equipment

The impairment of certain property, plant and equipment for production of medicines is based on the valuation of the recoverable amount with reference to the expected future cash flows estimated by management. Judgment is required in estimating the expected future cash flows from the Group in connection to an in-house manufactured product under the trade name of JinErLun. If the actual future cash flows are less than expected, additional impairment may be required. An impairment loss of nil (2009: US$805,000) was recognised in profit or loss in the consolidated statement of comprehensive income. The carrying amount of the relevant property, plant and equipment as at 31 December 2010 is US$516,000 (2009: US$659,000) (see note 14).

Deferred tax assets

As at 31 December 2010, a deferred tax asset of US$4,431,000 (2009: US$1,432,000) in relation to unrealised profits on inventories and impairment loss on property, plant and equipment has been recognised in the Group's consolidated statement of financial position. The recognition of the deferred tax asset mainly depends on whether sufficient future profits or taxable temporary differences will be available in the future. In cases where the actual future taxable profits generated are less than expected, a material reversal of deferred tax assets may arise, which would be recognised in the profit and loss account in the period in which such a reversal takes places.

4. KEY SOURCES OF ESTIMATION UNCERTAINTY - continued

Impairment of goodwill

Determining whether goodwill is impaired requires an estimation of the value in use of the cash-generating units to which goodwill has been allocated. The value in use calculation requires the Group to estimate the future cash flows expected to arise from the cash-generating unit and a suitable discount rate in order to calculate the present value. Where the actual future cash flows are less than expected, a material impairment loss may arise. As at 31 December 2010, the carrying amount of goodwill is US$379,000 (2009: US$379,000). Details of the recoverable amount calculation are disclosed in note 19.

Impairment of trade receivables

On assessing any impairment of the Group's trade receivables, the management regularly reviews the recoverability, creditworthiness of customers and ages of the trade receivables. Impairment on trade receivables is made on the estimation of the future cash flows discounted at an effective interest rate. If the financial condition of the customers of the Group deteriorates, additional impairment may be required. As at 31 December 2010, the carrying amounts of trade receivables (net of allowance for bad and doubtful debts) and allowance for bad and doubtful debts are US$30,394,000 (2009: US$20,746,000) and US$215,000 (2009: US$213,000) respectively.

5. TURNOVER AND SEGMENT INFORMATION

Turnover represents the net amount received and receivable for goods sold during the year.

The Group determines its operating segments based on the internal reports reviewed by the Board of Directors of the Company that are used to resources allocation and assessment of segment performance.

No analysis of the Group's assets and liabilities by operating segments is disclosed as it is not regularly provided to the chief operating decision maker for review.

5. TURNOVER AND SEGMENT INFORMATION - continued

The Group has the following two reportable operating segments:

(1) Marketing, promotion and sale of pharmaceutical products - marketing, promotion and sale of in-licensed medicine and pharmaceutical products from overseas and domestic pharmaceutical companies to wholesale customers across China, including distributors and hospitals; and

(2) Other business - production and sales of other medicines and pharmaceutical products to wholesale customers across China, including distributors and hospitals and production and sales of medical instruments.

The segment information is as follows:

For the year ended 31 December 2010

	Marketing, promotion and sale of pharmaceutical products US$'000	Others US$'000	Elimination US$'000	Consolidated US$'000
External segment revenue	130,687	1,490	-	132,177
Inter-segment revenue	-	1,569	(1,569)	-
Revenue	130,687	3,059	(1,569)	132,177
Segment results	76,873	1,229	-	78,102
Other gains and losses				373
Selling expenses				(30,966)
Listing expenses				(2,960)
Administrative expenses				(9,466)
Finance costs				(617)
Share of result of an associate				112
Share of result of a jointly controlled entity				56
Profit before taxation				34,634

5. TURNOVER AND SEGMENT INFORMATION - continued

For the year ended 31 December 2009

	Marketing, promotion and sale of pharmaceutical products	Others	Elimination	Consolidated
	US$'000	US$'000	US$'000	US$'000
External segment revenue	93,752	2,702	-	96,454
Inter-segment revenue	-	2,100	(2,100)	-
Revenue	93,752	4,802	(2,100)	96,454
Segment results	58,419	2,439	-	60,858
Other gains and losses				662
Selling expenses				(24,840)
Administrative expenses				(7,399)
Research and development costs				(2,038)
Finance costs				(390)
Share of results of associates				30
Share of result of a jointly controlled entity				43
Profit before taxation				26,926

Inter-segment revenue are conducted at prices and terms mutually agreed amongst those reportable segments.

The accounting policies of the reportable segments are the same as the Group's policies described in note 3. Segment results for the marketing, promotion and sale of pharmaceutical products and other business reportable segments represented the gross profit of the relevant operations. This is the measure reported to the chief operating decision maker for the purposes of resource allocation and performance assessment.

5. TURNOVER AND SEGMENT INFORMATION - continued

Other segment information

	Amounts included in the measure of segment results: Marketing, promotion and sale of pharmaceutical products	Others	Unallocated amounts	Total
	US$'000	US$'000	US$'000	US$'000
For the year ended 31 December 2010				
Depreciation and amortisation	839	399	325	1,563
Allowances for inventories	-	222	-	222
For the year ended 31 December 2009				
Depreciation and amortisation	1,115	391	507	2,013
Allowances for inventories	-	10	-	10

The Group primarily operates in the PRC. All revenue for external customers are attributed to the PRC and all non-current assets of the Group are located in the PRC.

Revenue from major products

The following is an analysis of the Group's revenue from its major products:

	2010	2009
	US$'000	US$'000
Deanxit	52,341	44,468
Ursofalk	35,879	28,327
Nesiritide	12,576	7,253
Exacin	10,632	-
Augentropfen Stulln Mono eye-drops	8,445	6,146
GanFuLe	4,219	4,780
Salofalk	3,989	1,824
Bioflor	1,266	-
Cystistat	738	515
Others	2,092	3,141
Total	132,177	96,454

6. OTHER GAINS AND LOSSES

	2010 US$'000	2009 US$'000
Net exchange loss	(729)	(405)
Government subsidies (Note)	391	801
Interest income	505	329
Gain on disposal of a subsidiary	-	24
Loss on disposal of an associate	-	(70)
Fair value change on investments held for trading	172	81
Gain on disposal of property, plant and equipment	1	7
Impairment loss recognised on property, plant and equipment (Note 14)	-	(805)
Discount on acquisition of an associate (Note 17)	-	647
Others	33	53
	373	662

Note: The amount represents the incentive subsidies provided by the PRC local authorities to the Group to reimburse the research and development expenditure incurred in the prior year. There are no specific conditions attached to the grants, the Group recognised the grants upon receipts.

7. FINANCE COSTS

	2010 US$'000	2009 US$'000
Interest on bank borrowings wholly repayable within five years	327	43
Imputed interest on deferred consideration payables	290	347
	617	390

8. DIRECTORS' AND EMPLOYEES' EMOLUMENTS

	2010 US$'000	2009 US$'000
Directors' fees	186	161
Other emoluments to non-executive directors and independent non-executive directors	-	-
Other emoluments to executive directors		
- basic salaries and allowances	309	340
- retirement benefits scheme contributions	13	15
	508	516

Details of emoluments paid by the Group to the directors are as follows:

	2010 US$'000	2009 US$'000
Mr. Lam Kong		
- directors' fee	23	23
- basic salaries and allowances	93	87
- retirement benefits scheme contributions	2	7
	118	117
Mr. Chen Hong Bing		
- directors' fee	23	23
- basic salaries and allowances	94	89
- retirement benefits scheme contributions	3	3
	120	115
Ms. Hou Xiao Xuan		
- directors' fee	23	23
- basic salaries and allowances	-	50
- retirement benefits scheme contributions	5	2
	28	75
Ms. Chen Yan Ling		
- directors' fee	23	23
- basic salaries and allowances	76	67
- retirement benefits scheme contributions	3	3
	102	93

8. DIRECTORS' AND EMPLOYEES' EMOLUMENTS - continued

	2010 US$'000	2009 US$'000
Mr. Hui Ki Fat		
- directors' fee	23	23
- basic salaries and allowances	46	47
- retirement benefits scheme contributions	-	-
	69	70
Mr. Paul Bernard Harper		
- directors' fee	8	23
- basic salaries and allowances	-	-
- retirement benefits scheme contributions	-	-
	8	23
Mr. Stuart Hamilton Leckie		
- directors' fee	27	23
- basic salaries and allowances	-	-
- retirement benefits scheme contributions	-	-
	27	23
Mr. Peng Huaizheng		
- directors' fee	15	-
- basic salaries and allowances	-	-
- retirement benefits scheme contributions	-	-
	15	-
Mr. Wu Chi Keung		
- directors' fee	12	-
- basic salaries and allowances	-	-
- retirement benefits scheme contributions	-	-
	12	-
Mr. Cheung Kam Shing, Terry		
- directors fee	9	-
- basic salaries and allowances	-	-
- retirement benefits scheme contributions	-	-
	9	-
Total	508	516

8. DIRECTORS' AND EMPLOYEES' EMOLUMENTS - continued

The five highest paid individuals for the year ended 31 December 2010 and 2009 included three and four directors respectively, details of whose emoluments are set out above. The emoluments of the remaining individual for the years were as follows:

	2010	2009
	US$'000	US$'000
Employees		
- basic salaries and allowances	146	71
- retirement benefits scheme contributions	3	3
	149	74

The emoluments of the employee were within the following bands:

	Number of employees	
	2010	2009
Up to HK$1,000,000	2	1

During the year, no emoluments were paid by the Group to the directors or the two highest paid individuals (including directors and employees) as an inducement to join or upon joining the Group or as compensation for loss of office. None of the directors has waived any emoluments during the year.

9. TAXATION

	2010 US$'000	2009 US$'000
Current tax:		
PRC Enterprise Income Tax	6,397	5,443
Hong Kong Profits Tax	187	97
Other jurisdictions	6	6
	6,590	5,546
Overprovision in prior years		
PRC Enterprise Income Tax	(11)	(11)
Deferred taxation (note 20):		
- Current year	(2,636)	561
Taxation charge for the year	3,943	6,096

The provision for PRC Enterprise Income Tax is based on the estimated taxable income for PRC taxation purposes at the rate of taxation applicable to each year.

Under the Law of the People's Republic of China on Enterprise Income Tax (the "EIT Law") and Implementation Regulation of the EIT Law, the tax rate of the PRC subsidiaries is 25% from 1 January 2008 onwards.

For the year ended 31 December 2010, the Enterprise Income Tax rate of Shenzhen Kangzhe Pharmaceutical Company Limited ("Kangzhe Shenzhen") and 深圳市康哲醫藥科技開發有限公司 (Shenzhen Kangzhe Pharmaceutical Technology Development Company Limited) ("Kangzhe Pharmaceutical Technology") was increased from 20% to 22% (2009: 18% to 20%).

Certain PRC subsidiaries are eligible for certain tax concession in the PRC. Pursuant to relevant laws and regulation, Kangzhe (Hunan) Medical Co. Ltd. ("Kangzhe Hunan") is entitled to a tax reduction to 15% for three years starting from 1 January 2006 granted by the local tax authority. Starting from 1 January 2009, Kangzhe Hunan is entitled to such a tax concession under annual renewal basis. For the year ended 31 December 2010, Kangzhe Hunan continued to entitle to a tax reduction to 15% (2009: 15%). Starting from 1 January 2010, 常德康哲醫藥有限公司 (Changde Kangzhe Pharmaceutical Co., Ltd.) ("Kangzhe Changde") is entitled to a tax reduction to 15% granted by the local tax authority and such tax concession is subject to renewal by the relevant tax bureau annually.

9. TAXATION - continued

Pursuant to the Labuan Offshore Business Activity Tax Act 1990 ("Labuan Tax Act") in Malaysia, CMS Pharmaceutical Agency Co., Ltd. ("CMS Pharmaceutical Agency") is eligible to elect to pay a lump sum taxation charge of MYR 20,000 (equivalent to approximately US$6,000) or 3% on net audited profits. For the years ended 31 December 2010 and 2009, CMS Pharmaceutical Agency elected to pay a lump sum tax.

Hong Kong Profits Tax is calculated at 16.5% of the estimated assessable profit for both years.

The taxation for the year can be reconciled to the profit before taxation per the consolidated statements of comprehensive income as follows:

	2010 US$'000	2009 US$'000
Profit before taxation	34,634	26,926
Tax at the applicable tax rate (Note)	7,619	5,385
Tax effect of share of result of a jointly controlled entity	(25)	(9)
Tax effect of share of results of associates	(12)	(6)
Tax effect of expenses that are not deductible in determining taxable profit	1,162	575
Tax effect of income that is not taxable in determining taxable profit	(59)	(52)
Tax effect of tax losses not recognised	83	223
Tax effect of tax concession	(11)	(28)
Effect on different applicable tax rates of subsidiaries	(457)	(280)
Effect of tax benefit arising from Labuan Tax Act	(4,718)	(629)
Overprovision in prior years	(11)	(11)
Utilisation of tax loss previously not recognised	(11)	-
Deferred tax arising from withholding tax on undistributed profit of a PRC subsidiary	359	925
Others	24	3
Taxation charge for the year	3,943	6,096

Note: The applicable PRC Enterprise Income Tax rate of 22% (2009: 20%) is the prevailing tax rate in Shenzhen, the PRC, where the operations of the Group are substantially based and the taxation charge mainly represents income tax of Kangzhe Shenzhen.

10. PROFIT FOR THE YEAR

	2010 US$'000	2009 US$'000
Profit for the year has been arrived at after charging:		
Directors' remuneration		
Fees	186	161
Other emoluments	309	340
Pension costs	13	15
	508	516
Other staff costs	13,501	13,082
Pension costs	777	674
Key employee benefit expense (note 39)	104	451
Total staff costs	14,890	14,723
Auditor's remuneration	165	150
Allowance for bad and doubtful debts	18	57
Allowance for inventories	222	10
Release of prepaid lease payments	67	7
Depreciation of property, plant and equipment	724	898
Amortisation of intangible assets (included in cost of goods sold)	839	1,115
Cost of inventories recognised as an expense	52,821	34,078
Minimum lease payment under operating lease in respect of property	620	621

11. DIVIDENDS

	2010 US$'000	2009 US$'000
Dividend paid		
Interim dividend for 2009 of US$0.10 per share on 47,408,904 shares	-	4,741
Final dividend for 2009 of US$0.10 (2008: US$0.10) per share on 47,408,904 (2008: 47,246,376) shares	4,741	4,725
	4,741	9,466
Dividend proposed		
Proposed final dividend for 2010 of US$0.013 (2009: US$0.10) per share of par value of US$0.005 (2009: US$0.10) on 1,143,691,000 (2009: 47,408,904) shares	14,868	4,741

During the year, a dividend of US$0.10 per ordinary share of par value of US$0.10 (2009: US$0.10) totaling US$4,741,000 was paid to shareholders as the final dividend for the year ended 31 December 2009 (2009: US$4,725,000 for the year ended 31 December 2008).

The Board of Directors propose to declare a final dividend of US$0.013 per ordinary share of par value of US$0.005 for the year ended 31 December 2010 (2009: US$0.10 per ordinary share of par value of US$0.10).

12. DISTRIBUTION

	2010 US$'000	2009 US$'000
Distribution of one Healthlink Consultancy Inc. ("Healthlink") share per one ordinary share with par value of US$0.10 of the Company in December 2009 (note 35(a))	-	8,681
Cash dividend	-	1,969
	-	10,650

13. EARNINGS PER SHARE

The calculation of the basic and diluted earnings per share attributable to the owners of the Company is based on the following data:

	2010 US$'000	2009 US$'000
Earnings for the purposes of basic and diluted earnings per share (profit attributable to owners of the Company)	30,587	20,684

	Number of ordinary shares As at 31 December 2010	 2009
Weighted average number of ordinary shares for the purpose of basic earnings per share	999,419,110	946,290,084
Effect of dilutive potential ordinary shares on share options	12,607,889	5,132,705
Weighted average number of ordinary shares for the purpose of diluted earnings per share	1,012,026,999	951,422,789

The number of shares for the purpose of calculating basic and diluted earnings per share for the years ended 31 December 2010 and 2009 have been adjusted to reflect the share sub-division (see note 30) effective on June 2010.

14. PROPERTY, PLANT AND EQUIPMENT

	Buildings	Leasehold improvement	Plant and machinery	Motor vehicles	Furniture, fixtures and equipment	Construction in progress	Total
	US$'000	US$'000	US$'000	US$'000	US$'000	US$'000	US$'000
COST							
At 1 January 2009	2,646	189	3,562	1,836	1,334	-	9,567
Currency realignment	2	-	4	2	1	-	9
Additions	-	-	108	127	45	-	280
Disposals	-	-	(32)	(409)	(24)	-	(465)
Disposal of a subsidiary	-	-	-	-	(12)	-	(12)
Distribution of a subsidiary	-	-	(926)	-	(57)	-	(983)
At 31 December 2009	2,648	189	2,716	1,556	1,287	-	8,396
Currency realignment	82	6	85	50	36	1	260
Additions	-	-	26	166	87	75	354
Disposals	-	-	-	(75)	(167)	-	(242)
At 31 December 2010	2,730	195	2,827	1,697	1,243	76	8,768
DEPRECIATION							
At 1 January 2009	1,039	94	1,575	672	728	-	4,108
Currency realignment	1	-	2	1	1	-	5
Provided for the year	135	63	291	262	147	-	898
Eliminated on disposals	-	-	(30)	(305)	(17)	-	(352)
Disposal of a subsidiary	-	-	-	-	(6)	-	(6)
Distribution of a subsidiary	-	-	(600)	-	(37)	-	(637)
Impairment loss recognised (note)	-	-	805	-	-	-	805
At 31 December 2009	1,175	157	2,043	630	816	-	4,821
Currency realignment	38	5	66	23	25	-	157
Provided for the year	123	33	163	259	146	-	724
Eliminated on disposals	-	-	-	(66)	(150)	-	(216)
At 31 December 2010	1,336	195	2,272	846	837	-	5,486
CARRYING VALUES							
At 31 December 2010	1,394	-	555	851	406	76	3,282
At 31 December 2009	1,473	32	673	926	471	-	3,575

Note: During the year ended 31 December 2009, the directors conducted a review of certain of the Group's property, plant and equipment for production of medicines and determined that these plant and machinery were impaired. An impairment loss of US$805,000 (see note 6) was recognised in profit or loss in the consolidated statement of comprehensive income. The impairment was due to deteriorating demand in the medicines produced. The recoverable amount of the plant and machinery was determined based on a value-in-use calculation. For impairment test purpose, the calculation uses cash flow projections for the operation of production of medicines based on financial budgets approved by the management covering a five-year period at a discount rate of 15%. As at 31 December 2010, the recoverable amount of the relevant property, plant and equipment is greater than the carrying values. Therefore, no additional impairment loss was recognised in profit or loss in the current year.

14. PROPERTY, PLANT AND EQUIPMENT - continued

The property, plant and equipment are depreciated over their estimated useful lives as follows:

Buildings	Over the shorter of the relevant lease terms, or 4.75%
Leasehold improvement	Over the shorter of the relevant lease terms, or 2%
Plant and machinery	18%
Motor vehicles	18%
Furniture, fixtures and equipment	18%

15. PREPAID LEASE PAYMENTS

	2010 US$'000	2009 US$'000
The Group's prepaid lease payments comprise:		
Leasehold land in the PRC:		
Medium-term leases	3,210	267
Analysed for reporting purposes as:		
Current asset (included in trade and other receivables)	68	7
Non-current asset	3,142	260
	3,210	267

16. INTEREST IN A JOINTLY CONTROLLED ENTITY

	2010 US$'000	2009 US$'000
Cost of unlisted investment in a jointly controlled entity	-	-
Share of post-acquisition profits and other comprehensive income	99	43
	99	43

16. INTEREST IN A JOINTLY CONTROLLED ENTITY - continued

As at 31 December 2010 and 31 December 2009, the details of the jointly controlled entity are as follows:

Name of jointly controlled entity	Place of establishment and business	Attributable interest held by the Group	Principal activity
廣東蘭太康虹醫藥有限公司 (Guangdong Lan Tai Kanghong Pharmaceutical Ltd.) ("Guangdong Lantai")	PRC	55% (note)	Distribution of medicine

Note: In November 2007, the Group acquired a 55% equity interest in Guangdong Lantai for nil consideration from a third party. The Group holds 55% of the registered share capital of Guangdong Lantai and has the power to appoint three out of the five directors of Guangdong Lantai. The remaining shareholding is held by one independent shareholder. However, under Guangdong Lantai's memorandum and articles of association, the power to govern the financial and operating policies rests with the Board of Directors of Guangdong Lantai and it requires two-third of the directors to approve the respective policies. The directors of the Company consider that the Group does not have control over Guangdong Lantai and has classified Guangdong Lantai as a jointly controlled entity.

The summarised financial information in respect of the Group's jointly controlled entity which is accounted for using equity method is set out below:

	2010 US$'000	2009 US$'000
Total assets	1,106	782
Total liabilities	(925)	(704)
Net assets	181	78
Group's share of net assets of a jointly controlled entity	99	43

	2010 US$'000	2009 US$'000
Turnover	1,419	1,179
Profit for the year	98	121
Group's share of result of a jointly controlled entity	56	43

17. INTEREST IN AN ASSOCIATE

	2010 US$'000	2009 US$'000
Cost of unlisted investments in an associate	1,687	1,687
Share of post-acquisition losses and other comprehensive income, net of dividends received	(256)	(180)
	1,431	1,507

As at 31 December 2010 and 31 December 2009, the details of the associate are as follows:

Name of associate	Place of establishment/ incorporation	Attributable interest held by the Group	Principal activities
Ophol Limited ("Ophol")	Hong Kong	24.49% (note 2)	Investment holding and provision of agency service

Notes:

(1) In December 2009, the associate, 深圳市深科醫療器械技術開發有限公司 (Shenzhen Shenke Medical Instrument Technological Development Limited), was disposed of to an independent third parties and a related company (note 37) for a consideration of RMB1,235,000 and RMB1,765,000 (equivalent to approximately US$181,000 and US$258,000) respectively and loss on disposal of US$70,000 was recognised in profit or loss.

(2) On 20 February 2009, the Group entered into an agreement (the "Ophol Agreement") with the controlling shareholder of Ophol to acquire its equity interest of 73.47% in Ophol for a consideration of RMB22,500,000 (equivalent to approximately US$3,295,000). In which, RMB18,000,000 (equivalent to approximately US$2,636,000) was paid at initial and the rest RMB4,500,000 (equivalent to approximately US$659,000) would be paid over four years beginning from 2010. Before the completion of the transaction under the Ophol Agreement, on 15 March 2009, the Group entered into separate agreements (the "March Agreements") with each of the other two original shareholders of Ophol. Pursuant to the two March Agreements, the Group transferred 24.49% equity interest in Ophol to each of the other two original shareholders of Ophol for the consideration of RMB7,500,000 (equivalent to approximately US$1,098,000) each. Upon the completion of the March Agreements, the Group holds 24.49% equity interest in Ophol, while the other two original shareholders of Ophol hold equity interest of 38.78% and 36.73% respectively. On the same date, the Group entered into a supplementary agreement with the controlling shareholder of Ophol, the other two original shareholders of Ophol, Ophol and Qingdao League Pharmaceutical Co., Ltd. ("Qingdao League") for the purpose to ratify the terms of the Ophol Agreement and the March Agreements.

17. INTEREST IN AN ASSOCIATE - continued

All the transactions mentioned above were completed in June 2009. As a result of all the agreements above, the Group in substance acquired 24.49% equity interest in Ophol for a consideration of RMB7,500,000 (equivalent to approximately US$1,098,000). In which, RMB6,000,000 (equivalent to approximately US$879,000) was paid at initial and the rest RMB1,500,000 (equivalent to approximately US$219,000) would be paid over four years beginning from 2010.

The holding of 24.49% equity interest in Ophol was classified as an associate of the Group and discount on acquisition of US$647,000 is recognised in the profit or loss for the year ended 31 December 2009.

The summarised financial information in respect of the Group's associate is set out below:

	2010 US$'000	2009 US$'000
Total assets	5,844	6,154
Total liabilities	1	-
Net assets	5,843	6,154
Group's share of net assets of an associate	1,431	1,507

	2010 US$'000	2009 US$'000
Turnover	462	2,170
Profit for the year	457	178
Other comprehensive expense	(20)	(3)
Group's share of results of associates for the year	112	30
Group's share of other comprehensive expense of associates	(5)	(1)

18. INTANGIBLE ASSETS

	Exclusive distribution right US$'000 (Note a(i))	Exclusive agency right US$'000 (Note b)	Total US$'000
COST			
At 1 January 2009	951	7,403	8,354
Exchange adjustments	1	-	1
At 31 December 2009	952	7,403	8,355
Exchange adjustments	25	-	25
Adjustment (note a(ii))	(261)	-	(261)
At 31 December 2010	716	7,403	8,119
AMORTISATION			
At 1 January 2009	(288)	(491)	(779)
Charge for the year	(294)	(821)	(1,115)
At 31 December 2009	(582)	(1,312)	(1,894)
Exchange adjustments	(18)	-	(18)
Charge for the year	(99)	(740)	(839)
At 31 December 2010	(699)	(2,052)	(2,751)
CARRYING VALUES			
At 31 December 2010	17	5,351	5,368
At 31 December 2009	370	6,091	6,461

18. INTANGIBLE ASSETS - continued

(a) Exclusive distribution right

(i) On 9 March 2008, the Group entered into an exclusive distribution agreement and a supplementary agreement (the "Nesiritide Agreements") with 西藏諾迪康藥業服份有限公司 (Tibet Rhodiola Pharmaceutical Holding Co., Ltd.) ("Rhodiola") in connection to a finished drug product (Lyophilized Recombinant Human Brain Natriuretic Peptide) which is distributed in the PRC market since 2005 under the trade name of Nesiritide for a term of three years with effect from 1 July 2008 to 30 June 2011.

Pursuant to the Nesiritide Agreements, the Group has obtained the exclusive distribution right of Nesiritide for nil consideration and has committed to handle the Phase IV clinical trials of Nesiritide for 2,000 cases in the PRC to meet the drug safety standards set by the Food and Drug Administration in the PRC ("SFDA"). The drug, Nesiritide, to be used in the 2,000 case clinical trials will be provided by Rhodiola free of charge. All other costs of the 2,000 case clinical trials should be borne by the Group. The management of the Group estimates the total costs to be incurred for completion of the 2,000 case clinical trials would be approximately RMB6,500,000 (equivalent to approximately US$919,000).

In the opinion of the directors of the Company, the Group obtained the exclusive distribution right of Nesiritide on the basis that the Group should complete the clinical trials of Nesiritide and bear all the costs of the clinical trials. Therefore, the costs to be incurred in clinical trials of US$919,000 are capitalised as an intangible asset with corresponding liability recognised during the year ended 31 December 2008.

The expected useful life of the exclusive distribution right of Nesiritide is 3 years.

(ii) During the year ended 31 December 2010, the Company completed the 2,000 clinical trials and actual cost was below the estimate, an adjustment of RMB1,755,000 (equivalent to approximately US$261,000) against the carrying amount of the related intangible asset. The adjustment has resulted in a decrease in the amortisation for the year of US$224,000.

18. INTANGIBLE ASSETS - continued

(b) Exclusive agency right

On 26 April 2008, a transfer agreement was entered into between Ophol, Qingdao League and Pharma Stulln GmbH ("Pharma"), the supplier of Augentropfen Stulln Mono ("Stulln") in Germany in connection to the transfer of the exclusive agency right of Stulln in the PRC from Qingdao League to Ophol at nil consideration. After Ophol has obtained the exclusive agency right of Stulln in the PRC, Ophol agreed to transfer such exclusive agency right to the Group on condition that the 51% equity interest of Qingdao League owned by Kangzhe Shenzhen would be transferred to Qingdao Leatu Trading Ltd., a company which has common shareholder with Ophol under the sale and purchase agreement. On 15 July 2008, the Group entered into a supplementary agreement with Ophol and Pharma in connection to the transfer of exclusive agency right of Stulln, from Ophol to CMS Pharmaceutical Agency, a wholly-owned subsidiary of the Company, at a consideration of RMB60,000,000 (equivalent to approximately US$8,779,000). CMS Pharmaceutical Agency will pay annually of RMB6,000,000 (equivalent to approximately US$878,000) to Ophol over the next ten years to settle the consideration. The directors of the Group recognise the payable as a deferred consideration (see note 28) in the amount of US$6,775,000, which represents the present value of the consideration of US$878,000 over next 10 years discounted at 5%. CMS Pharmaceutical Agency has replaced Qingdao League as the exclusive agent of Stulln for Pharma in the PRC from 1 August 2008 to 31 July 2018.

The expected useful life of the exclusive agency right is 10 years.

19. GOODWILL

	US$'000
At 1 January 2009	581
Released on disposal of a subsidiary	(202)
At 31 December 2009 and 31 December 2010	379

For the purposes of impairment testing, the entire amount of goodwill has been allocated to a cash generating unit ("CGU") representing a subsidiary in the marketing, promotion and sale of pharmaceutical products segment which is engaged in distribution and import of drug.

The recoverable amount of the CGU is determined from value in use calculations. The key assumptions for the value in use calculations are those regarding the discount rates, growth rates and expected changes to selling prices and direct costs during the year. Management estimates discount rates using pre-tax rates that reflect current market assessments of the time value of money and the risks specific to the CGU. The growth rates are based on industry growth forecasts. Changes in selling prices and direct costs are based on past performance and expectations of future changes in the market.

At 31 December 2010 and 31 December 2009, the Group performed impairment review for goodwill based on the cash flow projections which was derived from the financial budgets approved by the management covering a three-year period with discount rate of 10% (2009: 15%). For impairment review purpose, the cash flow projections was extrapolated for two years to a five-year period based on the assumption that no growth is expected after the third year. Another key assumption for the value in use calculation is the budgeted gross margin, which is determined based on the unit's past performance and management's expectation for the market development. The directors of the Company consider that no impairment loss on goodwill should be recognised.

20. DEFERRED TAX

The following are the deferred tax assets (liabilities) recognised and movements thereon during the current and prior years:

	Unrealised profits on inventories US$'000	Undistributed profits of PRC subsidiary US$'000	Others (note) US$'000	Total US$'000
At 1 January 2009	1,073	(839)	-	234
Credit (charge) to profit or loss for the year (note 9)	244	(925)	120	(561)
Exchange differences	(5)	-	-	(5)
At 31 December 2009	1,312	(1,764)	120	(332)
Credit (charge) to profit or loss for the year (note 9)	3,019	(359)	(24)	2,636
Exchange differences	-	-	4	4
At 31 December 2010	4,331	(2,123)	100	2,308

Note: These mainly represent the deferred tax assets recognised in relation to impairment loss on plant and machinery used for production of medicines for the year ended 31 December 2009 as explained on note 14.

The following is the analysis of the deferred tax balances for financial reporting purposes:

	2010 US$'000	2009 US$'000
Deferred tax assets	4,431	1,432
Deferred tax liabilities	(2,123)	(1,764)
	2,308	(332)

At 31 December 2010, the Group has unused tax losses of approximately US$2,611,000 (2009: US$2,178,000) available for offsetting against future profits. No deferred tax asset has been recognised in respect of such tax losses due to the unpredictability of future profit streams. Included in unrecognised tax losses at 31 December 2010 are tax losses of approximately US$1,327,000 (2009: US$1,378,000) that will expire within 5 years from the year of originating. Other tax losses may be carried forward indefinitely.

Under the EIT Law of PRC, withholding tax is imposed on dividends declared in respect of profits earned by PRC subsidiaries from 1 January 2008 onwards. Deferred taxation has been provided for in the consolidated financial statements in respect of temporary differences attributable to accumulated profits of the PRC subsidiary amounting to US$42,460,000 (2009: US$35,280,000).

21. INVENTORIES

	2010 US$'000	2009 US$'000
Raw materials	102	222
Work in progress	3	32
Finished goods	15,873	10,806
	15,978	11,060

22. TRADE AND OTHER RECEIVABLES

	2010 US$'000	2009 US$'000
Trade receivables	30,609	20,959
Less: Allowance for bad and doubtful debts	(215)	(213)
	30,394	20,746
Bills receivables	12,059	9,513
Purchase prepayment	2,264	56
Other receivables and deposit	4,597	2,479
Total trade and other receivables	49,314	32,794

The Group normally allows a credit period ranging from 0 to 90 days to its trade customers, but longer credit period up to four months was allowed to some selected customers.

An aging analysis of the trade receivables (net of allowance for bad and doubtful debts) presented based on the invoice date at the respective reporting period is as follows:

	2010 US$'000	2009 US$'000
0 - 90 days	26,940	17,879
91 - 365 days	3,424	2,839
Over 365 days	30	28
	30,394	20,746

22. TRADE AND OTHER RECEIVABLES - continued

The bills receivables of the Group are of the age within six months at the end of the reporting period.

Management closely monitors the credit quality of trade and other receivables and considers the trade and other receivables that are neither past due nor impaired to be of a good credit quality.

Included in the Group's trade receivables balance are debtors with aggregate carrying amount of US$5,457,000 (2009: US$4,476,000) which are past due at the reporting date for which the Group has not provided for impairment loss. Based on the historical experiences of the Group, trade receivables past due but not impaired are generally recoverable. The Group does not hold any collateral over these balances.

The following is an aging analysis of trade receivables which are past due but not impaired:

	2010 US$'000	2009 US$'000
0 - 90 days	2,406	2,274
91 - 365 days	3,025	2,174
Over 365 days	26	28
	5,457	4,476

The Group has provided full impairment for receivables that are due over 3 years because historical experience is such that receivables that are past due beyond 3 years are generally not recoverable.

Movement in the allowance for bad and doubtful debts:

	2010 US$'000	2009 US$'000
Balance at beginning of the reporting period	213	221
Impairment losses recognised on receivables	18	57
Amount written off as uncollectible	(16)	(65)
Currency realignment	-	-
Balance at end of the reporting period	215	213

Included in the allowance for bad and doubtful debts are individually impaired trade receivables with an aggregate balance of US$215,000 (2009: US$213,000) which have either been placed under liquidation or in severe financial difficulties. The Group does not hold any collateral over these balances.

23. AMOUNT DUE FROM A JOINTLY CONTROLLED ENTITY

Included in amount due from a jointly controlled entity amounting to US$498,000 (2009: US$312,000) is trade nature and is aged within three months. The Group allows a credit period of three months to its jointly controlled entity. The remaining amount is unsecured, non-interest-free and repayable on demand.

24. HELD FOR TRADING INVESTMENTS

	2010	2009
	US$'000	US$'000
Held for trading investments include:		
- Equity securities listed in the PRC	38	31

25. BANK BALANCES AND CASH/PLEDGED BANK DEPOSITS

The bank deposits and pledged bank deposits carry interest at the prevailing market rate of approximately 0.36% to 2.25% (2009: 0.36% to 1.71%) per annum.

As at 31 December 2010, included in pledged bank deposits amounting to US$1,716,000 (2009: US$17,380,000) represent deposits pledged to banks to secure short-term bank borrowings (see note 27). The remaining pledged bank deposits amounting to US$2,707,000 (2009: nil) and US$107,000 (2009: US$261,000) represent deposits pledged to banks to secure the issuance of letters of credit and foreign currency forward contracts respectively. Therefore the pledged bank deposits are classified as current assets.

26. TRADE AND OTHER PAYABLES

An aging analysis of the trade payables presented based on the invoice date at the end of the reporting period as follows:

	2010 US$'000	2009 US$'000
0 - 90 days	232	6,067
91 - 365 days	3	5
Over 365 days	8	7
	243	6,079
Payroll and welfare payables	2,746	2,239
Other tax payables	140	926
Other payables and accruals	5,123	1,818
	8,252	11,062

The credit period on purchases of goods is ranging from 0 to 120 days.

27. BANK BORROWINGS - SECURED

	2010 US$'000	2009 US$'000
Advanced from banks on discounted bills receivables	2,780	-
Import trade loans	-	7,557
Bank loans	1,481	8,960
	4,261	16,517
Carrying amount repayable within one year	4,261	16,517

The above bank borrowings are denominated in US$. Advanced from banks on bills receivables and import trade loans with carrying amount of US$2,780,000 (2009: nil) and nil (2009: US$7,557,000) respectively, carried fixed interest at a range from 1.39% to 1.98% (2009: 1.53% to 1.87%) per annum.

The remaining bank loans with carrying amount of US$1,481,000 (2009: US$8,960,000) bear interest at a range from LIBOR to LIBOR + 0.35% per annum. The range of effective interest rates (which are also equal to contracted interest rates) on the bank loans was from 1.11% to 1.52% (2009: 0.58% to 1.62%) per annum.

The bank borrowings are secured by the Group's pledged bank deposits amounting to US$1,716,000 (2009: US$17,380,000) (see note 25).

28. DEFERRED CONSIDERATION PAYABLES

	2010 US$'000	2009 US$'000
Non-current	4,627	5,291
Current	1,198	838
	5,825	6,129

During the year ended 31 December 2008, the Group acquired an agency right from Ophol which has become the associate of the Group during the year ended 31 December 2009 for a consideration of RMB60,000,000 (equivalent to approximately US$8,779,000) (see note 18(b)). The consideration is payable annually of RMB6,000,000 (equivalent to approximately US$878,000) for 10 years commencing on 26 April 2008. The present value of the discounted consideration determined based on a discount rate of 5% amounting to US$6,775,000 was accounted for by the Group as deferred consideration payable at initial recognition. As at 31 December 2010, the carrying value amounting to US$5,657,000 (2009: US$5,966,000) is included in deferred consideration payables.

The remaining deferred consideration payables represented consideration for the acquisition of an associate, Ophol (see note 17(2)).

29. DERIVATIVE FINANCIAL INSTRUMENTS

Derivative under hedge accounting

	2010 US$'000	2009 US$'000
Cash flow hedges		
- Interest rate swaps	24	74
- Foreign currency forward contracts	24	71
	48	145

(i) Interest rate swaps

The Group uses interest rate swaps to minimise its exposure to interest expenses of certain of its floating-rate US dollar bank borrowings by swapping floating interest rates to fixed interest rates. The interest rate swaps and the corresponding bank borrowings have the same terms and the directors of the Company considered that the interest rate swaps are highly effective hedging instruments. Major terms of the interest rate swaps are set out below:

At 31 December 2010

Notional amount	Maturity	Swaps
US$1,481,000	9 February 2011	From 3 - month LIBOR to 1.68%

At 31 December 2009

Notional amount	Maturity	Swaps
US$3,765,000	28 September 2010	From 1-month LIBOR + 0.35% to 1.47%
US$1,470,000	29 November 2010	From 3-month LIBOR + 0.35% to 1.68%
US$1,617,000	14 December 2010	From 3-month LIBOR + 0.35% to 1.68%
US$2,108,000	30 December 2010	From 3-month LIBOR + 0.35% to 1.68%

29. DERIVATIVE FINANCIAL INSTRUMENTS - continued

Derivative under hedge accounting - continued

(ii) Foreign currency forward contracts

At the end of the reporting period, the Group had the following foreign currency forward contracts designated as highly effective hedging instruments in order to manage the Group's foreign currency exposure in relation to US dollar interest and principal payments of its US dollar bank borrowings.

The terms of the foreign currency forward contracts have been negotiated to match the terms of the respective designated hedged items. Major terms of the foreign currency forward contracts are as follows:

At 31 December 2010

Notional amount	Maturity	Exchange rates
Buy US$1,510,000	9 February 2011	US$1: RMB6.699

At 31 December 2009

Notional amount	Maturity	Exchange rates
Buy US$2,140,000	23 August 2010	US$1: RMB 6.822
Buy US$3,821,000	28 September 2010	US$1: RMB 6.858
Buy US$1,470,000	2 December 2010	US$1: RMB 6.638
Buy US$1,620,000	14 December 2010	US$1: RMB 6.719
Buy US$2,140,000	30 December 2010	US$1: RMB 6.686

30. SHARE CAPITAL

	Number of shares '000	Amount US$'000
Authorised share capital:		
At 1 January 2009 and 31 December 2009	1,000,000	100,000
Increase in authorised share capital (note 3)	19,000,000	-
At 31 December 2010	20,000,000	100,000
Issued and fully paid:		
At 1 January 2009	47,246	4,725
Issue of shares to Key Employee Benefit Scheme (note 1)	162	16
At 31 December 2009	47,408	4,741
Issue of shares to Key Employee Benefit Scheme (note 1)	12	1
Issue of shares in consideration of acquisition of additional interest in a subsidiary (note 2)	264	26
Share sub-division (note 3)	906,007	-
Issue of shares on 28 September 2010 (note 4)	170,000	850
Issue of shares on 25 October 2010 (note 5)	20,000	100
At 31 December 2010	1,143,691	5,718

Notes:

(1) On 31 July 2009 and 14 May 2010, 162,528 and 11,835 new ordinary shares of US$0.10 of the Company were issued at GBP1.68 per share (equivalent to US$2.78 per share) and GBP5.99 per share (equivalent to US$8.8 per share) respectively for cash to the trust under the Key Employee Benefit Scheme (the "Scheme") (see note 39).

(2) On April 2010, pursuant to sales and purchase agreement entered on 19 April 2010, the Company issued 263,833 new ordinary shares of the Company of US$0.10 as the consideration for the acquisition of additional 40% equity interest in Sky United from Mr. Hui Ki Fat, a director and shareholder of the Company. The fair value of the ordinary shares of the Company was determined using the market price at the date of acquisition.

30. SHARE CAPITAL - continued

Notes: - continued

(3) Pursuant to the resolutions of the shareholders passed on 25 June 2010 and effective on 28 June 2010, each issued and unissued share in the share capital of the Company of a par value of US$0.10 was sub-divided into 20 new shares of a par value of US$0.005 each. Effective from 28 June 2010, the authorised and issued share capital of the Company is 20,000,000,000 ordinary shares of a par value of US$0.005 each and 953,691,440 ordinary shares of a par value of US$0.005 each respectively.

(4) On 28 September 2010, the Company issued 170,000,000 shares of US$0.005 each for cash pursuant to the global offering at the price of HK$5.06 each.

(5) On 25 October 2010, the Company issued 20,000,000 shares of US$0.005 each for cash under the over-allotment option pursuant to the global offering at the price of HK$5.06 each.

All the shares which were issued by the Company during the year ended 31 December 2010 and the year ended 31 December 2009 rank pari passu with each other in all respects.

31. SHARE OPTIONS

The Company granted share options of 708,695 shares with an exercise price of GBP1.38 per share on 26 June 2007. These options were granted to Evolution Securities China Limited ("Evolution"), the underwriters of the Company on the Company's initial public offering on AIM, in exchange for a payment of GBP1.00 from Evolution to the Company. These options are exercisable over a period of five years and vested on 26 June 2007. The share options will expire on 25 June 2012. The estimated fair value per share of these options is GBP0.4019 (equivalent to US$0.8046) with a total fair value of US$570,000. In addition to the share options granted to Evolution on successful basis, the Company paid an underwriting commission of US$1,151,000 (equivalent to GBP575,000) to Evolution representing 5.75% to the gross proceeds of the new issue. Such underwriting commission of US$1,151,000 settled in cash was recognised in the share premium account together with other listing expenses allocated to the new issued shares.

On 9 March 2009, Mr. Chen Hong Bing, a director of the Company, acquired the share options of 708,695 shares from Evolution. There was no other movement in the share options for both years.

On 28 June 2010, pursuant to the terms of the share options, the exercisable shares and exercise price had been adjusted to 14,173,900 shares and GBP0.069 per share respectively to reflect the share sub-division (note 30).

32. RESERVES

Capital reserve

Capital reserve resulted from transactions between the Group and its shareholders. It mainly represents equity shares of Kangzhe Shenzhen granted by Mr. Lam Kong to certain employees for their services rendered in prior year, rights granted by Mr. Lam Kong to certain employees to receive cash at a pre-determined formula for their services rendered in prior year, waiver of an advance to the Company by Mr. Lam Kong in 2006, discount on acquisitions of additional interest in subsidiaries from Mr. Lam Kong in 2004 and 2005, the difference between the transfer of the entire interest in Kangzhe Shenzhen to Sino Talent Limited ("Sino Talent") pursuant to the group restructuring in 2005 and the nominal value of Kangzhe Shenzhen's share capital, and difference between the par value of shares issued by the Company for the entire interest in CMS International Limited ("CMS International") and Healthlink pursuant to the group reorganisation in 2006 and the nominal value of the issued share capital of CMS International and Healthlink in preparation for the listing of the Company's shares. The balance was reduced by the capitalisation issue in 2007. The equity shares and rights granted by Mr. Lam Kong to certain employees had been terminated.

During the year ended 31 December 2010, the Group acquired additional interest in Sky United. An amount of US$2,221,000, representing the excess of the fair value of the new ordinary shares issued by the Company (note 30) over the decrease in the carrying value of the non-controlling interest is charged to capital reserve. The remaining amount of US$632,000, representing deemed distribution to a shareholder in respect of corporate exercise expenses borne by the Company.

Surplus reserve fund

Articles of Association of the Group's subsidiaries established in the PRC require the appropriation of certain percentage of their profit after taxation each year to the surplus reserve fund until the balance reaches 50% of the registered capital of the relevant subsidiaries. In normal circumstances, the surplus reserve fund shall only be used for making up losses, capitalisation into registered capital and expansion of the subsidiaries' production and operation. For the capitalisation of surplus reserve fund into registered capital, the remaining amount of such reserve shall not be less than 25% of the registered capital.

33. CAPITAL RISK MANAGEMENT

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

The capital structure of the Group consists of cash and cash equivalents, bank borrowings and equity attributable to owners of the Company, comprising issued share capital and reserves including accumulated profits.

The directors of the Company review the capital structure on a regular basis. As part of this review, the directors consider the cost of capital and the risks associated with each class of capital. Based on recommendations of the directors, the Group will balance its overall capital structure through the payment of dividends and new share issues.

34. FINANCIAL INSTRUMENTS

Categories of financial instruments

	2010 US$'000	2009 US$'000
Financial assets		
Loans and receivable (including cash and cash equivalents)	181,643	63,494
Held-for-trading financial assets	38	31
Financial liabilities		
Derivative instruments in designated hedge accounting relationship	(48)	(145)
Others financial liabilities measured at amortised cost	(10,960)	(29,771)

Financial risk management objectives and policies

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

34. FINANCIAL INSTRUMENTS - continued

Financial risk management objectives and policies - continued

Market risk

Interest rate risk

The Group's fair value interest rate risk is the risk that the fair value of a fixed rate financial instrument will fluctuate because of changes in market interest rates. Cash flow interest rate risk is the risk that the future cash flows of a financial instrument will fluctuate because of changes in market interest rates. In order to keep borrowings at fixed rate and to minimise the cash flow interest rate risk, the Group uses floating to fixed interest rate swaps to manage the cash flow interest rate risk exposure associated with the bank borrowings amounting to US$1,481,000 (2009: US$8,960,000) carrying at floating rates (see note 27 and note 29(i) for details) and therefore no sensitivity analysis is provided. Interest rate swaps, fixed rate bank balances and bank borrowings expose the Group to fair value interest rate risk.

Currency risk

Some subsidiaries of the Company have foreign currency purchases, which also expose the Group to foreign currency risk. Approximately 81.7% (2009: 76.4%) of the Group's purchases are denominated in currencies other than the functional currency of the group entities making the purchase. All sales of the Group are denominated in functional currency of the group entities making the sale.

The Group has entered into appropriate hedging instruments, mentioned in note 29(ii) to hedge against the potential currency risk arising from US$ denominated bank borrowings. The Group reviews the continuing effectiveness of hedging instruments at least at the end of each reporting period and until the hedging instrument expires or is terminated or the hedge no longer meets the criteria for hedge accounting. It is the Group's policy to negotiate the terms of the ledged derivatives to match the terms of the lodged item to maximize hedged effectiveness (see note 29 (ii) for details).

34. FINANCIAL INSTRUMENTS - continued

Financial risk management objectives and policies - continued

Market risk - continued

Currency risk - continued

The carrying amounts of the Group's foreign currency denominated monetary assets (representing bank balances) and monetary liabilities (representing trade and other payables and bank borrowings of which the foreign currency exposures are not hedged with hedging instruments) at the reporting date are as follows:

		Assets		Liabilities	
	Currency	2010	2009	2010	2009
		US$'000	US$'000	US$'000	US$'000
US dollars	US$	461	595	4,261	9,628
Euro	EURO	475	316	-	1,719
HK dollars	HK$	30,054	140	-	-

Management conducts periodic review of exposure and settlements of various currencies, and will consider hedging significant foreign currency exposures should the need arise.

The Group is mainly exposed to currency risk of the Euro, the US$ and HK$. The following table details the Group's sensitivity to a 1% (2009: 7%) increase and decrease in the RMB against the relevant foreign currencies. The sensitivity analysis includes only outstanding foreign currency denominated monetary items and adjusts their translation at the year end for a 1% (2009: 7%) change in foreign currency rates. The sensitivity analysis includes bank balances, trade and other payables and import trade loans without any hedging instruments. A positive number below indicates an increase in post-tax profit for the year where the RMB strengthens 1% (2009: 7%) against the relevant currency. If there is a 1% (2009: 7%) weakening in RMB against the relevant foreign currencies, there would be an equal and opposite impact on the result for the year:

	2010	2009
	US$'000	US$'000
US dollars	38	632
Euro	(4)	98
HK dollars	(301)	-

34. FINANCIAL INSTRUMENTS - continued

Financial risk management objectives and policies - continued

Market risk - continued

Other price risk

The Group's held-for-trading investments in listed securities are measured at fair value at each reporting date with reference to the listed share prices. Therefore, the Group is exposed to equity price risk and the management will monitor the price movements and take appropriate actions when it is required. The exposure of the equity price risk is minimal and no sensitivity to equity price risk is provided.

The Group is also exposed to other price risk through its investments in derivative financial instruments. The Group's other price risk is mainly concentrated on the foreign exchange forward contracts entered during the year.

The sensitivity analyses have been determined based on the exposure to other price risks for derivative at the reporting date. If the forward rate of the foreign exchange forward contracts had been 5% higher/lower and all other variables were held constant, the fair value changes which deferred in equity as hedging reserve for the year ended 31 December 2009 and 2010 would increase/decrease by US$558,000 and US$76,000 respectively.

Credit risk

The Group's maximum exposure to credit risk in the event of the counterparties failure to perform their obligations as at 31 December 2010 in relation to each class of recognised financial assets is the carrying amount of those assets as stated in the consolidated statements of financial position. In order to minimise the credit risk, management of the Group has delegated a team responsible for determination of credit limits, credit approvals and other monitoring procedures to ensure that follow-up action is taken to recover overdue debts. In addition, the Group reviews the recoverable amount of each individual trade debt at the end of the reporting period to ensure that adequate impairment losses are made for irrecoverable amounts. In this regard, the directors of the Company consider that the Group's credit risk is significantly reduced.

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

Other than concentration of credit risk on liquid funds which are deposited with several banks with good reputation, the Group has no significant concentration of credit risk on trade and other receivables, with exposure spread over a number of counterparties and customers and across diverse geographical areas.

34. FINANCIAL INSTRUMENTS - continued

Financial risk management objectives and policies - continued

Liquidity risk

In the management of the liquidity risk, the Group monitors and maintains a level of cash and cash equivalents deemed adequate by the management to finance the Group's operations and mitigate the effects of fluctuations in cash flows.

Ultimate responsibility for liquidity risk management rests with the board of directors, which has built an appropriate liquidity risk management framework for the management of the Group's short, medium and long-term funding and liquidity management requirements.

The following table details the Group's remaining contractual maturity for its non-derivative financial liabilities based on the agreed repayment terms. The table has been drawn up based on the undiscounted cash flows of financial liabilities based on the earliest date on which the Group can be required to pay. The table includes both interest and principal cash flows. To the extent that interest flows are floating rate, the undiscounted amount is derived from current interest rate at the end of the reporting period.

In addition, the following table details the Group's liquidity analysis for its derivative financial instruments. The tables have been drawn up based on the undiscounted contractual net cash (inflows) and outflows on derivative instruments that settle on a net basis, and the undiscounted gross (inflows) and outflows on these derivatives that require gross settlement. When the amount payable is not fixed, the amount disclosed has been determined by reference to the projected interest rates as illustrated by the interest rate existing at the end of the reporting period. The liquidity analysis for the Group's derivative financial instruments are prepared based on the contractual maturities as the management consider that the contractual maturities are essential for an understanding of the timing of the cash flows of derivatives.

34. FINANCIAL INSTRUMENTS - continued

Financial risk management objectives and policies - continued

Liquidity risk - continued

	Repayable on demand or less than 1 year US$'000	1 to 5 years US$'000	Over 5 years US$'000	Total undiscounted cash flows US$'000	Carrying amount at 31 December 2010 US$'000
As at 31 December 2010					
Trade and other payables	874	-	-	874	874
Deferred consideration payables	1,157	3,750	2,018	6,925	5,825
Fixed interest rate borrowings	2,780	-	-	2,780	2,780
Variable interest rate borrowings	1,482	-	-	1,482	1,481
	6,293	3,750	2,018	12,061	10,960
Derivatives - net settlement					
Foreign currency forward contracts	24	-	-	24	24
Derivatives - gross settlement					
Interest rate swaps					
- Inflow	(1)	-	-	(1)	
- Outflows	4	-	-	4	
	3	-	-	3	24

	Repayment on demand or less than 1 year US$'000	1 to 5 years US$'000	Over 5 years US$'000	Total undiscounted cash flows US$'000	Carrying amount at 31 December 2009 US$'000
As at 31 December 2009					
Trade and other payables	7,125	-	-	7,125	7,125
Deferred consideration payables	879	3,679	3,032	7,590	6,129
Fixed interest rate borrowings	7,682	-	-	7,682	7,557
Variable interest rate borrowings	9,014	-	-	9,014	8,960
	24,700	3,679	3,032	31,411	29,771
Derivatives - net settlement					
Foreign currency forward contracts	95	-	-	95	71
Derivatives - gross settlement					
Interest rate swaps					
- inflows	(53)	-	-	(53)	
- outflows	142	-	-	142	
	89	-	-	89	74

34. FINANCIAL INSTRUMENTS - continued

Fair value

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

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

- the fair value of derivative instruments is calculated using discounted cash flow analysis using the applicable yield curve for the duration of the instruments for non-optional derivatives; and

- the fair value of other financial assets and financial liabilities (excluding derivative instruments) is determined in accordance with generally accepted pricing models based on discounted cash flow.

The carrying amounts of financial assets and liabilities carried at amortised cost approximate to their respective fair values.

Fair value measurements recognised in the consolidated statement of financial position

The following table provides an analysis of financial instruments that are measured subsequent to initial recognition at fair value, grouped into Levels 1 to 2 based on the degree to which the fair value is observable.

- Level 1 fair value measurements are those derived from quoted prices (unadjusted) in active market for identical assets or liabilities.

- Level 2 fair value measurements are those derived from inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices).

	31 December 2010		31 December 2009	
	Level 1	Level 2	Level 1	Level 2
	US$'000	US$'000	US$'000	US$'000
Held-for-trading investments				
Listed equity securities	38	-	31	-
Derivative financial instruments	-	48	-	145

There were no transfers between Level 1 and 2 for the year ended 31 December 2010 and the year ended 31 December 2009.

35. DISPOSAL OF SUBSIDIARIES

(a) On 11 December 2009, the Board of Directors of the Company approved the payment of a dividend. The dividend is payable by way of a distribution in specie ("the Distribution") of the entire share capital of a wholly owned subsidiary, Healthlink, on the basis of one Healthlink share for every one ordinary share of the Company with par value of US$0.1 each in the capital of the Company, with cash dividend alternative. Healthlink and its subsidiaries ("Healthlink Group") is engaged in the research and development of medicine in the PRC.

On 15 December 2009, 17.9% shareholders elected for cash alternative and 82.1% shareholders elected to receive shares in Healthlink. Under a repurchase agreement between the Company and Healthlink, the 17.9% remaining Healthlink share held by the Company were repurchased by Healthlink for aggregate cash consideration of US$1,969,000. The 82.1% remaining Healthlink Shemes were distributed to the shareholders who elected to receive shares on Healthlink.

On 16 December 2009, the Company has made the Distribution of US$8,681,000, which is equivalent to the net asset value of Healthlink Group on that date, in the form of distribution in specie of the 38,921,747 ordinary shares of US$0.01 each, representing entire share capital of Healthlink, and cash dividend of US$1,969,000. The Distribution was made to the shareholders on the register of members on 27 November 2009.

The net assets of Healthlink at the date of the Distribution were as follows:

	11 December 2009
	US$'000
NET ASSETS DISTRIBUTED	
Property, plant and equipment	346
Other receivables	91
Bank balances and cash	8,099
Other payables	(185)
	8,351
Non-controlling interests	330
	8,681
Satisfied by:	
Interim dividend in specie	8,681
Cash outflow arising on the Distribution:	
Bank balances and cash distributed of	8,099
Cash dividend	1,969
	10,068

35. DISPOSAL OF SUBSIDIARIES - continued

During the year ended 31 December 2009, Healthlink has no contribution on the turnover and contributed loss which amounted to US$1,138,000 to the Group.

The loss for the year included other gains, administrative expenses and research and development costs of US$782,000, US$275,000 and US$1,645,000 for year ended 31 December 2009.

(b) On 17 December 2009, the Group disposed of a subsidiary, Shandong Baolihao, to the independent third parties. The net liabilities of Shandong Baolihao at the date of disposal were as follows:

	17 December 2009
	US$'000
NET LIABILITIES DISPOSED OF	
Property, plant and equipment	6
Inventories	107
Trade and other receivables	1
Bank balances and cash	1
Trade and other payables	(341)
	(226)
Attributable goodwill	202
	(24)
Gain on disposal	24
Total consideration	-
Cash outflow arising on disposal:	
Bank balances and cash disposed of	1

During the year ended 31 December 2009, Shandong Baolihao has contributed turnover amounting to US$15,000 and loss amounting to US$75,000 to the Group.

36. OPERATING LEASE

The Group as lessee

The Group's total future minimum lease payments under non-cancellable operating lease in respect of property which fall due as follows:

	2010 US$'000	2009 US$'000
Within one year	508	487
In the second to fifth years inclusive	275	390
	783	877

The lease is negotiated for a lease term of 1 to 5 years at fixed monthly rental.

37. RELATED PARTY TRANSACTIONS

(a) Apart from details of the balances with related parties disclosed in note 23, the Group entered into the following transactions with related parties during the year:

Name of related company	Relationship	Nature of transactions	2010 US$'000	2009 US$'000
Ophol	Associate	Finance cost	290	347
Guangdong Lantai	Jointly controlled entity	Sales of goods	1,238	743
Sunpharma Gmbh	Related company*	Purchase of goods	-	157
Shenzhou Kangzhe Industrial Investment Co. Ltd.	Related company*	Consideration received for disposal of interest in an associate	-	258
Hui Ki Fat	Director and shareholder	Consideration paid for acquisition of additional interest in a subsidiary	2,325	-

* Sunpharma GmbH and Shenzhen Kangzhe Industrial Investment Co. Ltd. are companies in which Mr. Lam Kong, the director and shareholder of the Company has beneficial and controlling interests.

37. RELATED PARTY TRANSACTIONS - continued

(b) The Group entered into the following banking facilities which were secured by personal guarantees executed by related parties during the year:

	2010 US$'000	2009 US$'000
Bank A (note i)		
- letters of credit and other facilities amount	-	11,606
- working capital facilities amount	-	4,394
	-	16,000
- letters of credit and other utilised amount	-	5,277
- working capital utilised amount	-	-
	-	5,277
Bank B (note ii)		
- letters of credit and other facilities amount	-	10,252
- working capital facilities amount	-	2,929
	-	13,181
- letters of credit and other utilised amount	-	1,648
- working capital utilised amount	-	-
	-	1,648

Notes:

(i) The banking facilities were secured by personal guarantees executed by a director, Mr. Lam Kong. The banking facilities were expired on 13 July 2010.

(ii) The banking facilities were secured by personal guarantees executed by the directors of the Company. Mr. Lam Kong, Mr. Chen Hongbing, Ms. Chen Yanling, Ms. Huo Xiaoxuan and personal guarantees executed by a director of Kangzhe Shenzhen, Ms. Sa Manlin. The Group terminated this banking facilities on 30 July 2010.

(c) The key management personnel includes solely the directors of the Company and the compensation paid to them is disclosed in note 8.

38. RETIREMENT BENEFITS SCHEMES

The employees employed in the PRC are members of the state-managed retirement benefit schemes operated by the PRC government. The PRC subsidiaries are required to contribute a certain percentage of their payroll to the retirement benefit schemes to fund the benefits. The only obligation of the Group with respect to the retirement benefit schemes is to make the required contributions under the schemes.

The employees employed in Hong Kong are required to join the Mandatory Provident Fund Scheme (the "MPF Scheme"). Contributions to the MPF Scheme are made in accordance with the statutory limits prescribed by the Mandatory Provident Fund Ordinance of Hong Kong.

During the year, the total expense recognised in the profit or loss for the above schemes amounted to US$790,000 (2009: US$689,000).

39. KEY EMPLOYEE BENEFIT SCHEME

The Scheme was adopted by the Board on 31 July 2009 ("Adoption Date"). Unless terminated earlier by the Board, the Scheme shall be valid and effective for a term of 20 years commencing on the Adoption Date. Pursuant to the rules of the Scheme, the Company set up a trust through a trustee (the "Trustee"), Fully Profit Management (PTC) Limited, for the purpose of administration the Scheme. A summary of some of the principal terms of the Scheme is set out in below.

(a) The purpose of the Scheme is to recognise the contributions by certain employees who have been actively involved in the business development of the Group and to establish and maintain a superannuation fund for the purpose of providing retiring allowances for certain employees (including without limitation employees who are also directors) of the Group, and to give incentive in order to retain them for the continual operation and development of the Group.

(b) Under the Scheme, the Board may, from time to time, at its absolute discretion and subject to such terms and conditions as it may think to select an employee (the "Member") who completed 10 years' services in the Group (subject to consent of the Board if the employee completed 5 year's services in the Group) for participation in the Scheme for 10 years after retirement (the "Payment Year") (subject to adjustment set out in (d) below).

(c) The Company will, on a yearly basis, contribute the sum equal to an amount not less than 0.5%, but no more than 3% of its after tax profits shown on the audited consolidated financial statements of the Group, or issue such number of shares of the Company to the Trustee in consideration of payment of such amount as the Board may determine with reference to the aforesaid contribution as against the then market value of the shares of the Company (the "Yearly Contributions"), subject to the Board's approval.

39. KEY EMPLOYEE BENEFIT SCHEME - continued

(d) The amount payable to the Members depends on the value of the assets held by the Trustee (the "Fund"). If the value of the Fund is less than the aggregate amount of contributions previously made by the Company, the amount payable to the Members and the Payment Year will be adjusted by a factor derived from the value of the Fund and the aggregate amount of contributions previously made by the Company. The only obligation of the Company is to make the Yearly Contributions to the Fund.

During the year ended 31 December 2010, the Company contributed cash amounting to US$104,000 (2009: US$451,000) to the Fund and which were recognised as key employee benefit expenses in the consolidated statement of comprehensive income. On the other hand, the Scheme subscribed 11,835 shares and 162,528 shares of the Company during the year ended 31 December 2010 and 31 December 2009 respectively (see note 30).

40. SUBSIDIARIES OF THE COMPANY

As at 31 December 2010 and 31 December 2009, the details of the Company's subsidiaries are set as follows:

Name of subsidiaries	Place of incorporation/ establishment and operation	Issue and fully paid share capital/registered capital		Equity interest held by the Group				Principal activities
		31 December 2010	31 December 2009	31 December 2010		31 December 2009		
				Directly	Indirectly	Directly	Indirectly	
CMS International (note 1)	British Virgin Islands	US$10,000	US$10,000	100%	-	100%	-	Investment holding
Kangzhe Hunan (Sino-Foreign Equity Joint Venture)	PRC	RMB20,000,000	RMB20,000,000	-	100%	-	100%	Production of medicines
Kangzhe Pharmaceutical Technology (Wholly-owned PRC Enterprise)	PRC	RMB10,000,000	RMB10,000,000	-	100%	-	100%	Investment holding
Kangzhe Pharmaceutical Industrial Ltd. (note 1)	British Virgin Islands	RMB21,288,000	RMB21,288,000	-	100%	-	100%	Investment holding
Kangzhe Shenzhen (Wholly-foreign owned Enterprise)	PRC	RMB350,000,000	RMB150,000,000	-	100%	-	100%	Distribution and import of drugs and medical devices
Sino Talent	Hong Kong	HK$1	HK$1	-	100%	-	100%	Investment holding
Sky United	Hong Kong	HK$10	HK$10	-	100%	-	60%	Trading of drugs
Kangzhe Changde (wholly-owned PRC Enterprise)	PRC	RMB2,000,000	RMB2,000,000	-	100%	-	100%	Trading of drugs
CMS Pharmaceutical Agency	Malaysia	US$1	US$1	-	100%	-	100%	Trading of drugs

Notes:

1. Being inactive subsidiaries, the place of operation is also in British Virgin Islands.

2. None of the subsidiaries had issued any debt securities at the end of the year.