2011 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 Branch
Industrial and Commercial Bank of China,
ShenZhen Branch
Hongkong and Shanghai Banking Corporation Limited

Registered Office
Maples Corporate Services Limited
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Cayman Islands

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Nanshan District
Shenzhen 518057
PRC

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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

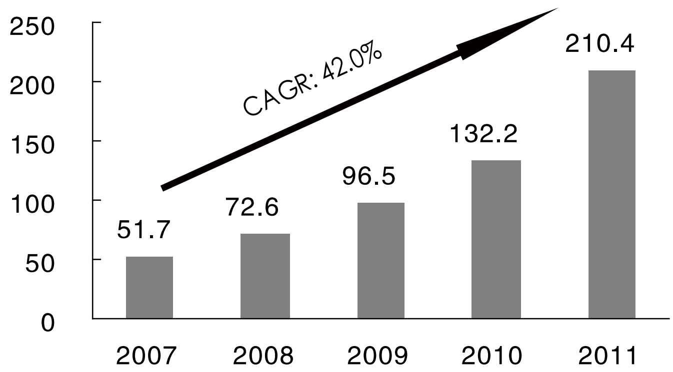
Stock Code
867

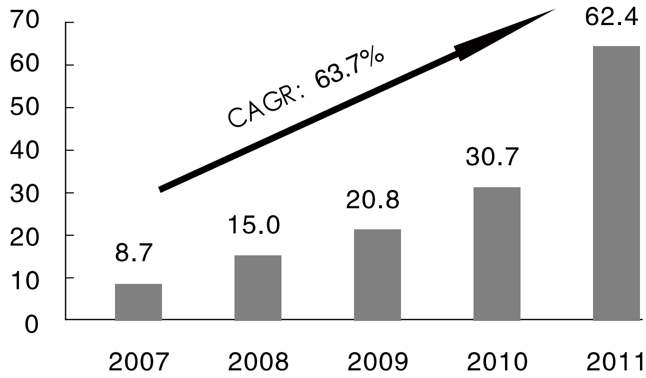
Company's website
www.cms.net.cn

Financial Highlights

- Turnover up 59.2% to US$210.4 million (2010: US$132.2 million)
- Profit for the year up 103.2% to US$62.4 million (2010: US$30.7 million)
- Basic earnings per share up 71.5% to US3.971 cents (2010: US2.315 cents)
- As at 31 December 2011, the Group's bank balances and cash were US$97.9 million while readily realizable bank acceptance bills amounted to US$23.6 million
- Proposed final dividend of US0.8 cent per share, making the total dividend for the year ended 31 December 2011 of US1.44 cent per share[1], representing an increase of 38.5% from 2010 (2010: final dividend and total dividend of US1.04 cent per share respectively[2])
- Proposed 1 bonus issue of share for every 2 shares held (2010: nil)

Turnover and profit of the Group for the latest five years are set out below:





Consolidated Balance Sheet Highlights

	As at 31 December				
	2007	2008	2009	2010	**2011**
	US$'000	US$'000	US$'000	US$'000	**US$'000**
Total assets	54,944	70,494	90,777	223,207	**474,167**
Total liabilities	13,100	17,773	36,843	23,218	**82,994**
Net assets	41,844	52,721	53,934	199,989	**391,173**

1. Total dividend of US1.44 cent per share for the year ended 31 December 2011 includes final dividend of US0.8 cent per share and interim dividend of US0.64 cent per share. Interim dividend has been adjusted to reflect the bonus issue effective in September 2011 as approved by Shareholders at the Extraordinary General Meeting held on 14 September 2011.
2. Both final dividend and total dividend of US1.04 cent per share for the year ended 31 December 2010 were adjusted to reflect the bonus issue effective in September 2011 as approved by Shareholders at the Extraordinary General Meeting held on 14 September 2011.

Chairman's Statement

Dear Shareholders,

On behalf of the Board of Directors, I would like to sincerely thank all of 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 of the Company and its subsidiaries (the "Group") for the year ended 31 December 2011 (the "Reporting Period")

Results Overview

The year 2011 was an important year for the Group. This year was not only filled with challenges and developments but it was also the first full fiscal year for the Group since its listing on the Main Board of the Hong Kong Stock Exchange ("HKEx"). During the year, the Group persisted in its strategic positioning and development direction as a marketing, promotion and sales service provider for prescription drugs in China, focused on the balance development between continuous products introduction and sales and promotion network expansion. In April 2011, the Group successfully extended its business model by acquiring Great Move Enterprises Limited ("Great Move") and its subsidiaries. The main wholly-owned subsidiary of Great Move is Tianjin Precede Medical Trade Development Co., Ltd. (officially renamed Tianjin Kangzhe Pharmaceutical Technology Development Co., Ltd., or "Tianjin Kangzhe", on 24 October 2011), a Chinese company that engaged in the marketing, promotion and sale of prescription drugs through the Agency Promotion Model in China. After the acquisition, the Group not only owns a well-established physician-orientated Direct Academic Orientated Promotion Model, but has also added the Agency Promotion Model, which is composed of independent third-party sales representatives or distributors. The Group will focus on integrating and developing the two sales and promotion models. In addition, in order to control the product rights of "Protein Hydrolysate", the Group acquired 51% equity interests of the manufacturer-Guangming Pharmaceutical Co., Ltd. (officially renamed the Guangxi Kangzhe Guangming Pharmaceutical Co., Ltd. or "Kangzhe Guangming", on 10 October 2011) in May 2011 by way of investment in capital and equity increase.

During the Reporting Period, despite the volatile conditions of Chinese pharmaceutical market, the Group achieved significant growth, with turnover amounting to US$210.4 Million (2010: US$132.2 million) representing an increase of 59.2% over last year, while profit attributable to owners of the Company reached US$62.3Million (2010: US$30.6 million), up 103.6% from last year. Basic earnings per share were US3.971 cents (2010: US2.315 cents).

Business Review

In 2011, uncertain policies and the downturn of Chinese pharmaceutical market resulted in unprecedented challenges for the pharmaceutical industry. During the volatile conditions of the Chinese pharmaceutical market in 2011, the Group still achieved satisfactory results growth, as a result of the right position and firm implementation of our two core strategies-the continuous introduction and development of products and expansion of` promotion and sales network.

Product Introduction and Development

In 2011, the Group remained committed to introducing and developing products. During the Reporting Period, while maintaining the steady growth of its two flagship products-Deanxit and Ursofalk-the Group also increased its investment and intensity of promotion on other potential products, organized over 1,000 academic activities at various levels, continuously advanced the formation of expert networks and brands, increased the number of prescription doctors, boosted the doctors' prescription volume and further strengthened the depth of coverage of products in hospitals. At the same time, the introduction of the Agency Promotion Model also broadened the scope and channel of the Group's product screening. During the Reporting Period, the Group not only continued products screening for the Direct Academic Orientated Promotion Network (the "Direct Network"), but also included screening for products suitable for the Agency Promotion Network (the "Agency Network").

For product introduction, the target of the Group remains to introduce an average of not less than two products annually with academic value to our Direct Network and two products with market potential to our Agency Network, at the same time the Group have adjusted the key direction of the product introduction. In 2011, the Group gave consideration to each of the three different product development strategies while favoring the strategy of gaining permanent control market rights of products, through payment of an upfront fee or licensing fee, or through collaboration with other companies to obtain products or the market rights of the products in China. Compared to the previous method of signing exclusive contracts, this method of introducing new products is more difficult, as the negotiation process is more complicated, and more time consuming, but once the negotiation is successful, the Group can obtain longer-term and more stable product rights to ensure its long-term stable development. In May 2011, the Group successfully in-licensed "Protein Hydrolysate". This is the first product that the Group obtained the market rights in China by equity control since the Hong Kong listing, and this is also the results of the combination of the two promotion models of the Group.

In addition, the Group already owns the product rights of Tyroseuleutide (CMS024) in China. Tyroseuleutide is used in the treatment of primary liver cancer and has huge potential market value in China. The Group has already commenced Tyroserleutide phase III clinical study in 2011. The title of the phase III study of Tyroserleutide being conducted now is "A Randomized, Double Blind, Placebo Controlled, Multicenter Phase III Study to Evaluate the Safety and Efficacy of Tyroserleutide for Injection in Patients With Hepatocellular Carcinoma", and the primary purpose of the study is to verify the efficacy of Tyroserleutide on prolonging recurrence-free survival ("RFS") and overall survival ("OS") of the patients with hepatocellular carcinoma. The clinical study will be conducted in 26 Class Three hospitals which are at the leading level of the liver cancer field in China. As at 31 December 2011, the Group has already successfully started kick-off meetings of Tyroserleutide phase III clinical trial during 18 hospitals in China, and has already enrolled 4 subjects. If the clinical trial can be smoothly completed, it will have a significant and positive impact on the Group`s performance in the future.

Meanwhile, the Group has already signed three products from late 2010 to early 2011 that require import drug registration in China, and the application of clinical trial for registration of Budenofalk has been accepted by the State Food and Drug Administration ("SFDA") during the first half of 2011. These three products are effective complements to our existing strong therapeutic departments, and after the completion of the import drug registration, the Group can make use of the existing promotion and sales network and expert resources to achieve rapid product coverage. Moreover, the Group has several other products under the negotiation process.

In the future, the Group will continue to consider each of the three product introduction strategies, and at the same time build up diversified approaches such as purchases or equity controls to acquire more stable product rights.

Network Expansion

During the Reporting Period, the Group continued to expand its marketing and promotion network, aside from expanding the geographical reach and hospital coverage of the promotion network, the Group also focused on integrating and developing the Direct Network and Agency Network. During the Reporting Period, the Group sales spanned over 14,600 hospitals throughout China, of which almost 8,600 hospitals were covered by the Direct Network and over 7,800 hospitals were covered by the Agency Network.

In 2011, through the "Internship Programme" and "Professional Talent Development Programme" the Group recruited nearly 300 premium undergraduate and post-graduate students from medical colleges throughout the country for internships, and through a large number of professional training and strict internal evaluations to select outstanding talents to join the Direct Network of the Group. At the year ended 31 December 2011, the number of marketing, promotion and sales professionals in the Direct Network of the Group had close to 1,200. In September 2011, the Group launched a new round of campus recruitment to unceasingly add new talents to the Direct Network of the Group. In addition, the Group also strengthened the social recruitment efforts during the Reporting Period.

In 2011, the Group has also refined the management of the Agency Network. By combining its years of academic experience in specialized construction with meticulous management to assisted Tianjin Kangzhe (formerly known as "Tianjin Precede Medical Trade Development Co., Ltd") to enhance its business competence and capabilities, and improved and refined the collaboration model of the market management department. The Group also assisted Tianjin Kangzhe to set up and improve its information management system and injected the Group's business and management system into it. With these efforts, Tianjin Kangzhe maintained stable performance and achieved steady sales growth despite the volatile environment and fierce competition in the Chinese pharmaceutical market observed in 2011. Meanwhile, the Group also strengthened the formation and expansion of the Agency Network. As at 31 December 2011, the number of independent third party sales representatives or distributors in the Agency Network of the Group had close to 1,000.

With the Chinese government healthcare policy favoring the rural market, the rural market and community hospitals will gradually become another emerging spotlight of China pharmaceutical development. In 2011, the Group followed the development of healthcare policy in China, and began to consider entering the rural market and gradually extending its marketing and promotion network within this market. On the one hand, the Group took advantage of the presence of the Agency Network in the rural market to continue to expand and penetrate its network, which effectively compensated for the void of the Direct Network in the rural market; on the other hand, the Group also took into consideration the recruitment of local sales staff to build local marketing and promoting teams in the rural market.

In addition, during the Reporting Period, the Group has also explored the advantage of integrating the two networks to accelerate the pace of market coverage and increase the sales of products. The task of promotion models integration for some products of the Group has already been initiated and achieved initial success.

During the Reporting Period, the Group also purchased a property at a preferential price offered by the Shenzhen Municipal Government, located at Majialong Industrial Zone Nanshan District, Shenzhen in China with the Block parcel number of 04-05-17 and named the Innovation Building*, with a gross floor area between 4,000 m^2 and 5,000 m^2. The property will be used as Corporate Headquarters of the Group and will fulfill the needs of the Group in its accelerated development and the recruitment of more talents. The property should satisfy the project completion and acceptance requirements within 24 months from September 2011, and submit the information of completion and acceptance. The property has to be transferred within 30 working days after obtaining the project acceptance record.

Cash Dividend and Bonus Issue

The Company paid an interim dividend of US 0.64 cent per ordinary share for the six months ended 30 June 2011 (adjusted to reflect the bonus issue effective in September 2011 as approved by Shareholders at the Extraordinary General Meeting held on 14 September 2011). The Board is delighted to recommend a final dividend of US 0.8 cent (equivalent to HK$0.0621) per ordinary share of the Company (each a "Share") for the year ended 31 December 2011 to shareholders whose names appear on the register of members of the Company at the close of business on Friday, 4 May 2012 (the "Record Date"). Payment of such final dividend in Hong Kong Dollars is expected to be made to the shareholders on Monday, 14 May 2012 after the shareholders' approval at the Annual General Meeting ("AGM") of the Company on Wednesday, 25 April 2012. The Board also recommends a bonus issue to the shareholders whose names appear on the register of members of the Company at the close of business on the Record Date on the basis of one (1) bonus share (the "Bonus Shares") for every two (2) existing Shares (the "Bonus Issue"). It is expected that the dealings in the Bonus Shares on the HKEx will commence on Tuesday, 15 May 2012 subject to the approval of the shareholders at the AGM and the HKEx. Details of the Bonus Issue are set out in the Management Discussion and Analysis section of the Annual Report.

Outlook and Future Development

Going forward, the Group will firmly continue to pursue two core development strategies-the continuous introduction and development of products and the expansion of marketing and promotion network.

For existing products, the Group will continue to maintain the stable growth of the flagship products and increase the investment in and intensify the promotion of potential products, thereby broadening the growth prospects. Meanwhile, in addition to sustainable investment into the academic promotion of products, the Group will also continue to make full use of the advantages of the two promotion models, accelerate the integration of marketing and promotion of products.

For product introduction, the Group will continue to carry out product selection and evaluation activities, to in-license products with competitive advantage, persevere to introduce an average of not less than two products suitable for the Direct Network and also to introduce an average of not less than two products suitable for the Agency Network per year. In addition to maintain the current long-term product agent strategy, the Group will also continue to diversify the way through which products are introduced to acquire more stable and sustainable product rights. Meanwhile, the Group will introduce products in a systematic manner in accordance with market demand, keep a close eye on the development of the China pharmaceutical policies, and systematically increase the screening of investment in high growth potential products, in order to enhance the competitiveness of the Group's future product portfolio.

**For Identification Only*

In relation to network development, the Group will continue to expand the scale of the Direct Network through new staff recruitment and to boost network coverage and market segmentation. At the same time, the Group will make full use of the characteristics of information management to strengthen the specialized construction and management refinement of the Agency Network, increase the number of agents and accelerate the network penetration in the rural market. In addition, the Group will also accelerate the complementary strengths of the two promotion networks and further extend the marketing and promotion presence of the Group at the rural market.

Aside from organic development, the Group will also continue to use capitalization as a development strategy, continue to improve the internal control of the Group and strengthen the management and control of the Group's subsidiaries.

The year 2011 was the most volatile year for the Chinese pharmaceutical market. Under numerous external pressures, the Group still achieved stable development. Going forward, the board will pay close attention to the changes in the environment of the Chinese pharmaceutical market, closely follow the direction of the China's pharmaceutical policies development, adjust the development strategy on a timely basis, and actively take measures to deal with the changes in market and policy. The Group will continue to work hard, seize new opportunities in a time of challenges and take practical measures in order to achieve even better results!

Chairman
Lam Kong
Shenzhen China
15 March, 2012

Management Discussion and Analysis

Business Review

During the Reporting Period, despite the volatile market conditions in China, the Group achieved significant growth. Turnover amounted to US$210.4 Million (2010: US$ 132.2 Million), representing an increase of 59.2% over the last year, while net profit reached US$62.4 Million (2010: US$30.7 Million), representing an increase of 103.2% over last year. Basic earnings per share were US3.971 cents (2010:US2.315 cents).

During the Reporting Period, the Group recorded satisfactory results growth as it benefited from the pursuit of two core development strategies: the introduction and development of products and expansion of its marketing and promotion network, in addition, the Group acquired products and expanded the network through merger and acquisition during the Reporting Period.

Product Development

During the Reporting Period, the Group marketed, promoted and sold in the China market: nine products via the Direct Network, ten products via the Agency Network, and also owned several products in-house manufactured. For Deanxit and Ursofalk, the top two sales contributors for the Group in the Reporting Period, the Group principally consolidated the existing market, continuously established new market segments and extended the rural market coverage to achieve stable growth. With regards to the products with market potential, the Group mainly focused on increasing investment in products promotion, development of hospital coverage and continued to expand prescription departments to achieve more extensive market growth of the products. The year 2011 was a very competitive year for the Agent Promotion Model. The two main products-Shaduolika and Yinuoshu under the Agency Network of the Group still successfully achieved steady growth even under the fierce market competition. This was mainly due to the successful exclusive bidding of Yinuoshu in the Essential Drug List tenders of some key markets during the Reporting Period, which contributed to its sales growth. Aside from the Agency Products, in May 2011, the Group also successfully gained the product rights of “Protein Hydrolysate” in the China market through equity control. That product was marketed, promoted and sold in the China market through the Agency Network, and the Group also supported the product on the academic front to enhance its academic positioning. This was the result of integrating the professional academic ability of the Direct Network and the rapid market coverage ability of the Agency Network. In addition, in January 2011, the Group and Tibet Rhodiola Pharmaceutical Holding Co.,Ltd. (“Tibet Pharma”), the manufacturer of XinHuoSu, successfully extended the exclusive agency agreement for XinHuoSu in the China market for another three years, which further consolidated the strategic partnership between each other.

To increase the transparency in the development of product portfolio and the visibility of future development, from the end of 2010 to the beginning of 2011, the Group signed agreements for three products-Budenofalk, L-lysine Aescinat and Thiotriazolin-which require import drug registration in China, and the application of clinical trial for registration of Budenofalk has been accepted by the SFDA in the first half of 2011. According to the relevant provisions of the SFDA, the registration process of a new drug will normally take between two to five years to complete, so it would take two to five years for such products to start to contribute to the Group's sales. All three products are effective complements to the Group's existing strong therapeutic departments, and after the completion of import drug registration, the Group can make use of the existing promotion and sales network and expert resources to achieve rapid product coverage. In addition, the phase III clinical trial of Tyroserleutide (CMS024), to which the Group has independent intellectual property rights, has already been commenced in 2011.

The Products of Direct Network

	Product Name	As a percentage of the Group's revenue (%)
Flagship Products	Deanxit (Flupentixol and Melitracen)	31.9
	Ursofalk (Ursodeoxycholic Acid)	22.0
Products with Market Potential	XinHuoSu (Nesiritide, Lyophilized Recombinant Human Brain Natriuretic Peptide, “rhBNP”)	8.7
	Augentropfen Stulln Mono Eye-drops (Esculin and Digitalisglycosides Eye-Drops)	4.7
	Salofalk (Mesalazine)	3.4
	Bioflor (Saccharomyces Boulardii)	2.3

(i) Flagship Products

Deanxit (Flupentixol and Melitracen)

Deanxit is manufactured by H. Lundbeck A/S of Denmark and is used for the treatment of mild to moderate depression and anxiety. Deanxit is our best-selling drug, and according to 2011 sales data from the China market provided by IMS Global Learning Consortium, Inc.(IMS), Deanxit was the most prescribed antidepressant medication in China. In 2011, Deanxit recorded sales of US$67.0 million, an increase of 28.1% when compared with last year, accounting for 31.9% of the Group's turnover. The Group's main objectives for Deanxit in 2011 were to continue to maintain and stabilize the existing market, vigorously expand into the rural market, and augment the coverage in the surrounding markets lacking the Group's presence. During the Reporting Period, the Group also created new growth by expanding the prescription departments of Deanxit, apart from continuing to strengthen and maintain its brand building in the traditional departments of neurology and psychiatry and the building of expert network, the Group also conducted marketing and promotion for Deanxit in the Gastrointestinal department. Moreover, Deanxit was included in the National Reimbursement Drug Lists in 2009, and the effect in advancing its sales has gradually come to light. During the Reporting Period, the sales coverage of Deanxit has spanned over 6,900 hospitals nationwide.

Ursofalk (Ursodeoxycholic Acid)

Ursofalk is manufactured by Dr. Falk Pharma GmbH of Germany and used for the treatment of cholesterol gallstones, cholestatic liver disease and bile reflux gastritis. According to 2011 sales data from the China market released by IMS, Ursofalk retained its first place ranking in the Ursodeoxycholic Acid ("UDCA") market. In 2011, Ursofalk recorded sales of US$46.2 million, an increase of 28.9% when compared with last year, and it accounted for 22.0% of the Group's turnover. Ursofalk is the Group's only drug which has been included on the National Essential Drugs List, and the Group paid close attention to the implementation and tenders of the National Essential Drugs List, and strengthened all aspects of the associated response tasks of the product such as tender and pricing, and successfully completed the tender of Ursofalk nationwide in the past year. In addition, the Group also strengthened the brand building of Ursofalk and the maintenance of its expert network, and systematically promoted the balanced development of Ursofalk in various therapeutic departments in the key and potential hospitals nationwide. During the Reporting Period, the Group also strengthened its efforts in the development and promotion of Ursofalk in medium-sized hospitals and rural hospitals in some areas. Due to the existence of other similar products in the market, and in order to consolidate the position of Ursofalk in the core hospitals nationwide, the Group selectively held many academic activities such as clinical trials and case studies in 150 core hospitals nationwide. During the Reporting Period, the sales coverage of Ursofalk spanned over 4,000 hospitals nationwide.

(ii) Products with Market Potential

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

XinHuoSu, manufactured by Tibet Pharma, is a biological agent used to treat acute heart failure patients who have dyspnea at rest or with minimal activity. During the Reporting Period, XinHuoSu recorded sales of US$18.4 million, representing an increase of 45.9% when compared with last year, and it accounted for 8.7% of the Group's turnover. During the Reporting Period, the Group was committed to further improving the regional distribution of XinHuoSu, and focused on cultivating the Eastern China market. On the basis of consolidating the existing indications, the Group also vigorously extended the use of the product in other departments such as the emergency department and cardiothoracic surgery department, which not only promoted the sales of XinHuoSu during the Reporting Period, but also laid a solid foundation for the development of XinHuoSu in the future. During the Reporting Period, the sales coverage of XinHuoSu spanned close to 1,000 hospitals nationwide.

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

Augentropfen Stulln Mono Eye-drops, manufactured by Pharma Stulln GmbH of Germany, is used to treat age-related macula degeneration and all forms of ocular asthenopia. During the Reporting Period, Augentropfen Stulln Mono Eye-drops recorded sales of US$9.8 million, representing an increase of 16.0% compared with last year, and it accounted for 4.7% of the Group's turnover. The core development strategies of Augentropfen Stulln Mono Eye-drops in 2011 were to strengthen brand building and to increase investment for promotion of the product at the key hospitals, to refine the indications of the product, and to actively carry out education of patients. During the Reporting Period, both the promotion and market demand for Augentropfen Stulln Mono Eye-drops in all the regions were quite positive, but it was restricted by the production capability of the manufacturer, resulting in a supply shortage in the market. During the Reporting Period, Pharma Stulln GmbH of Germany, the manufacturer of Augentropfen Stulln Mono Eye-drops, has promptly updated its production equipment and expanded the production line to ensure the adequate and timely supply to the Group. Augentropfen Stulln Mono Eye-drops is one of the potential products in which the Group has made a large investment, and it has much room for growth in the future. During the Reporting Period, the sales coverage of Augentropfen Stulln Mono Eye-drops spanned over 2,800 hospitals nationwide.

Salofalk (Mesalazine)

Salofalk is manufactured by Dr. Falk Pharma GmbH of Germany, including three dosage forms of coated tablets, suppositories and enemas, which are mainly used to treat ulcerative colitis and Crohn's Disease. During the Reporting Period, Salofalk recorded sales of US$7.1 million, representing an increase of 77.6% when compared with last year, and it accounted for 3.4% of the Group's turnover. The indication of Salofalk is inflammatory bowel disease, and this disease is presently in the under-diagnosis phase in China. Therefore, the most important mission of the Group for Salofalk was to improve the doctors' capability to recognize and diagnose of this condition, and to establish and develop the expert network and the brand image of Salofalk. During the Reporting Period, the Group once again held the CMS-Falk City Symposium, which invited a large number of domestic and international experts to share the prescription experience of Salofalk, and successfully launched the clinical trial of the Salofalk enema, and began the promotion of Salofalk enema nationwide. In the meantime, the Group has also focused on penetrating hospitals with this product. During the Reporting Period, the sales coverage of Salofalk spanned over 1,000 hospitals nationwide.

Bioflor (Saccharomyces Boulardii)

Bioflor, manufactured by Biocodex of France, is a biological agent used to treat adult and children diarrhea and diarrhea symptoms caused by the disturbance of intestinal flora. During the Reporting Period, Bioflor recorded sales of US$4.9 million, an increase of 284.1% when compared with last year, and it accounted for 2.3% of the Group's turnover. The year 2011 was the second year after the Group took over Bioflor, during which the major task of the Group was to penetrate hospitals. Meanwhile, during the Reporting Period, the Group strengthened the formation of its expert network of the product, and through a variety of academic activities and visits of front-line salespeople to doctors, it significantly improved the recognition and prescription rates of the doctors towards the product. In addition, during the Reporting Period, the Group also actively expanded the product's therapeutic departments, which gradually expanded the sales from a single department of pediatricians to the gastrointestinal department, and actively supported the sales growth of Bioflor.

(iii) Exacin (Isepamicin Sulfate Injection)

Exacin, manufactured by Asahi Kasei of Japan, is an aminoglycoside antibiotic product. During the Reporting Period, Exacin recorded sales of US$10.5 million, a slight decrease when compared with last year, and it accounted for 5.0% of the Group's turnover. Due to the national discussion on limiting the use of antibiotics in 2011, all hospitals throughout the country rigorously screened their directory of antibiotics, which led to a negative impact on the use of Exacin in hospitals.

(iv) Other Products

Apart from the products mentioned above, the Group also has two other products promoted by the Direct Network, which includes Cystistat (Sterile Hyaluronate Solution) and GanFuLe. During the Reporting Period, the two products contributed approximately 2.8% to the Group's turnover.

The Products of Agency Network

	Product Name	As a percentage of the Group's revenue (%) *
Flagship Products	Shaduolika (Yanhuning Injection)	7.4
	Yinuoshu (Ambroxol Hydrochloride for Injection)	7.7
Products with Market Potential	Protein Hydrolysate	0.5
	Kunning Oral Solution	0.3

*Note: Turnover from the Agency Network was only consolidated from 1 April 2011 to the end of 2011.

(i) Flagship Products

Shaduolika (Yanhuning Injection)

Shaduolika, developed and manufactured by Chongqing Yaoyou Pharmaceutical Co., Ltd., is a common injection of anti-infective traditional Chinese medicine used in pediatrics, respiratory and emergency treatment. During the Reporting Period, Shaduolika recorded sales of US$15.7 million, and it accounted for 7.4% of the Group's turnover. In 2011, the Group completed the re-assessment of the safety of Shaduolika, and held a summary convention in Guangzhou in which more than 200 clinicians participated, and thereby giving rise to the influence of Shaduolika among the clinicians.

Yinuoshu (Ambroxol Hydrochloride for Injection)

Yinuoshu is manufactured by TIPR Pharmaceutical Responsible Co., Ltd. It is the first generic version of an ambroxol hydrochloride for injection approved in China, and is an expectorant product used for respiratory diseases. During the Reporting Period, Yinuoshu recorded sales of US$16.3 million, and it accounted for 7.7% of the Group's turnover. During the Reporting Period, Yinuoshu won the exclusive tender from the National Essential Drugs List in many key areas, which greatly increased the coverage and sales of Yinuoshu in the hospitals of these areas.

(ii) Products with Market Potential

Protein Hydrolysate

"Protein Hrdrolysate" includes oral solution and granules, and is an exclusive product in China manufactured by Kangzhe GuangMing, which is a new generation short peptide enteral nutrition drug manufactured by the innovative Chinese Biochemical Technique. During the Reporting Period, the product recorded sales of US$1.1 million, and it accounted for 0.5% of the Group's turnover. The year 2011 was the year in which the Group introduced "Protein Hrdrolysate", and the Group set the key task for "Protein Hrdrolysate" in this year, which was to complete the preparation of various market foundation. During the Reporting Period, the Group successfully completed all coordination work on "Protein Hrdrolysate" between the Agency Network and Kangzhe GuangMing, continued to pay close attention to tendering, pricing and penetrating of key hospitals, and completed the product agency selection in the areas with low market presence. During the Reporting Period, "Protein Hrdrolysate" has been successfully listed on some provincial Insurance Reimbursement Drug Lists.

Kunning Oral Solution

Kunning Oral Solution, exclusively manufactured by Yantai Rongchang Pharmaceutical Co., Ltd., is used to promote blood circulation dissipate stasis, and promotes the involution of uterus. During the Reporting Period, Kunning Oral Solution recorded sales of US$0.7 million, and accounted for 0.3% of the Group's turnover.

(iii) Other Products

Apart from the products mentioned above, the Group also has other products promoted by the Agency Network, which includes Shenshuiqing, Supingshu, Irbesartan and Hydrochlorothiazide and so on. During the Reporting Period, the products listed above accounted for 1.3% of the Group's turnover.

Moreover, the Group also produced and sold 15 other in-house manufactured products, including JinErLun, Fufang Danshen Pian and Niuhuang Jiedu Pian and so on. During the year, the Group's in-house manufactured products accounted for 1.8% of the Group's turnover.

In-house Researched Pharmaceutical Product Development

Tyroseuleutide, researched and developed by the Group with independent intellectual property rights, is used to treat primary liver cancer and has huge potential market value in china, which will be an important product for the Group in the future. In 2011, the Group has fully initiated the phase III clinical trial of Tyroseuleutide. The title of the phase III study of Tyroserleutide is "A Randomized, Double Blind, Placebo Controlled, Multicenter Phase III Study to Evaluate the Safety and Efficacy of Tyroserleutide for Injection in Patients With Hepatocellular Carcinoma", and the primary purpose of the study is to verify the efficacy of Tyroserleutide on prolonging RFS and OS of the patients with hepatocellular carcinoma. The clinical trial was jointly launched by Zhaoyou Tang (Academician of the Chinese Academy of Engineering and President of Liver Cancer Research Institute, Fudan University, Shanghai) and Mengchao Wu (Academician of Chinese Academy of Sciences and President of The Second Military Medical University, Shanghai East Hepatobiliary Surgery Hospital), Shanghai Fudan University affiliated Zhongshan Hospital was set as the leading unit, with Professor Jia Fan acting as the lead researcher of the clinical trial. After thorough investigation of the available patient cases and the qualifications of the institutions, the clinical trial was set to include 26 leading liver cancer treatment tier three hospitals in China as collaboration partners. During the Reporting Period, the Group has already successfully started kick-off meetings of Tyroserleutide phase III clinical trial during 18 hospitals in China, and has already enrolled 4 subjects. In addition, the Group has purchased a parcel of land spanning 36,422.4 square meters in the new region of Pingshan, Shenzhen, China, with the plan of building a manufacturing facility which will be used to manufacture Tyroseuleutide and other products.

Network Development

During the Reporting Period, the Group made marked improvement of its marketing promotion network. Through the "Internship Programme" and "Professional Talent Development Programme", the Group recruited outstanding fresh graduates from medical colleges to join its Direct Network. Meanwhile, the Group has continued to expand the Agency Network, and selected additional high quality independent third party sale representatives or agents to join its growing Agency Network. In addition, the Group has paid more attention to the recruitment of experienced medical representatives. As of 31 December 2011, the Direct Network of the Group had close to 1,200 sales, marketing and promotion professionals while the Agency Network had close to 1,000 independent third party sales representatives or agents.

Aside from enlarging the number of sales representatives and agents, the Group has also expanded the network geographical coverage and hospital coverage. As of 31 December 2011, the sales coverage of the Group spanned over 14,600 hospitals throughout China, of which around 8,600 hospitals were covered by the Direct Network and over 7,800 hospitals were covered by the Agency Network.

In addition to network expansion, the Group has also continued to enhance the management of the Direct Network and refined the incentive mechanism for sales representatives, improved network organization and enhanced the operating efficiency of the network. Meanwhile, the Group refined the management of the Agency Network, and assisted Tianjin Kangzhe to build up an information management system, and introduced the Group's management and evaluation system into it. Meanwhile, the Group also combined both its abundant management experience and its high academic standards to improve the operational ability of Tianjin Kangzhe, and also aided Tianjin Kangzhe to improve and refine the collaboration model of the market management department.

During the Reporting Period, the Group vigorously expanded its rural market coverage. through the marketing and promotion network continued to penetrate the rural market to fill the Group's market absence in the rural market and to tap the existing potential of the rural market with expectations of further growth. Meanwhile, the Group actively utilized the advantages of the integration of both networks to accelerate its market coverage and to boost the sales of its products. During the Reporting Period, the task of promotion models integration for some products of the Group has already been initiated and achieved initial success.

Outlook and Future Development

Based on the result achieved in 2011, the Group will continue to strive for better results. On the one hand, the Group will step up the implementation of the three strategies for new product introductions, namely, the "Rapid-growth Products Strategy", "Long-term Prospects Products Strategy", and the "Permanent Control of Marketing Rights Strategy", and commit to improve the transparency, visibility and stability of product development, and endeavor to gain control of the products right in the China market; on the other hand, the Group will constantly expand its marketing promotion network and enhance the coverage of the marketing promotion network in the rural market. Meanwhile, the Group will continue to invest in the academic promotion of its products, enhance the management of the Agency Network, continue to strive at taking advantage of the synergy from the two promotion models, and accelerate the combination of both models and networks in product sales and promotion. Going forward, the Group will continue to utilize and make use of the potential of the capital market, take full advantage of and effectively consider the combination of the Chinese government's healthcare policies and development trends, correctly assess the situation, so the Group can achieve long-term and stable development with a more pragmatic and aggressive attitude and through a more diversified manner.

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 Report in accordance with international financial report standards, the financial performance are summarized as follows:

Acquisition of Subsidiaries

For the year ended 31 December 2011, the Group completed two equity acquisitions. In April 2011, the Group acquired a 100% equity interest in Great Move at a total consideration of approximately US$206.1 million. Since then, Great Move has become a wholly-owned subsidiary of the Group. In May 2011, the Group acquired a 51% equity interest in Kangzhe Guangming with a capital injection of US$4.6 million in order to obtain exclusive distribution rights to "Protein Hydrolysate". Since then, Guangxi Guangming has become a subsidiary of the Group.

Segment Information

There were two segments disclosed in the Group's Annual Report for the year ended 31 December 2010: (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. Since other business segment was immaterial, the management regarded it as no longer a segment in resources allocation and performance review, so the Group had no reportable operating segment for the year ended 31 December 2011.

Turnover

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

	2011		2010	
	US$'000	Weighted rate	US$'000	Weighted rate
Deanxit	67,046	31.9%	52,341	39.6%
Ursofalk	46,244	22.0%	35,879	27.1%
Nesiritide	18,352	8.7%	12,576	9.5%
Yinuoshu	16,269	7.7%	-	-
Shaduolika	15,657	7.4%	-	-
Exacin	10,505	5.0%	10,632	8.0%
Augentropfen Stulln Mono eye-drops	9,800	4.7%	8,445	6.4%
Salofalk	7,084	3.4%	3,989	3.0%
GanFuLe	4,874	2.3%	4,219	3.2%
Bioflor	4,863	2.3%	1,266	1.0%
Protein Hydrolysate	1,142	0.5%	-	-
Cystistat	1,106	0.5%	738	0.6%
Others	7,451	3.6%	2,092	1.6%
	210,393	100%	132,177	100%

Turnover increased by 59.2% from US$132.2 million for the year ended 31 December 2010 to US$210.4 million for the year ended 31 December 2011, mainly due to the sales volume increase, with relatively stable selling prices. Meanwhile, turnover of US$40.0 million was contributed by the subsidiaries newly acquired in 2011, and accounted for 19.0% of the Group's turnover.

Cost of Goods Sold

Cost of goods sold increased by 68.8% from US$54.1 million for the year ended 31 December 2010 to US$91.3 million for the year ended 31 December 2011, primarily reflecting growth in sales. Meanwhile, cost of goods sold of US$18.8 million generated from the subsidiaries newly acquired in 2011, accounted for 20.7% of the Group's cost of goods sold. Cost of goods sold of arisen from the amortization of intangible assets recognized on the acquisition of the subsidiaries in 2011 amounted to US$1.7 million.

Gross Profit and Gross Profit Margin

Gross profit increased by 52.5% from US$78.1 million for the year ended 31 December 2010 to US$119.1 million for the year ended 31 December 2011, primarily reflecting growth in turnover. Meanwhile, gross profit of US$19.5 million was contributed by the subsidiaries newly acquired in 2011, and accounted for 16.3% of the Group's gross profit. Gross profit margin decreased from 59.1% for the year ended 31 December 2010 to 56.6% for the year ended 31 December 2011, mainly due to a change in product mix, the import tax associated with increased intra-group transactions, the relatively lower gross profit margin of the subsidiaries newly acquired in 2011, and the effect of the amortization of intangible assets recognized on the acquisition of the subsidiaries in 2011.

Other Gains and Losses

Other gains and losses increased by 2,060.1% from US$0.4 million for the year ended 31 December 2010 to US$8.1 million for the year ended 31 December 2011, mainly reflecting gains arising from fluctuations in foreign exchange and interest income from higher bank balances. Meanwhile, other gains and losses of US$1.5 million was contributed by the subsidiaries newly acquired in 2011, and accounted for 18.2% of the Group's other gains and losses.

Selling Expenses and Selling Expenses as a Percentage of Turnover

Selling expenses increased by 38.7% from US$31.0 million for the year ended 31 December 2010 to US$43.0 million for the year ended 31 December 2011, primarily reflecting increased marketing and promotion expenses arising from the increased sales volume. Simultaneously, there was an increase in salaries and welfare for the Group's marketing and sales staff as a result of the increase in the number of sales staff. Meanwhile, selling expenses of US$2.1 million was generated from the subsidiaries newly acquired in 2011, and accounted for 4.8% of the Group's selling expenses. Selling expenses as a percentage of turnover decreased by 3.0 percentage points from 23.4% for the year ended 31 December 2010 to 20.4% for the year ended 31 December 2011 as the Group benefited from economies of scale, and the lower selling expenses as a percentage of turnover at the subsidiaries newly acquired in 2011.

Administrative Expenses and Administrative Expenses as a Percentage of Turnover

Administrative expenses increased by 62.0% from US$9.5 million for the year ended 31 December 2010 to US$15.3 million for the year ended 31 December 2011, mainly due to an increase in professional fee arising from acquisitions, and an increase in the business tax associated with the increase in intra-group transactions. Meanwhile, administrative expenses of US$2.3 million was generated from the subsidiaries newly acquired in 2011, and accounted for 15.0% of the Group's administrative expenses. Administrative expenses as a percentage of turnover increased by 0.1 percentage points from 7.2% for the year ended 31 December 2010 to 7.3% for the year ended 31 December 2011.

Finance Costs

Finance costs increased by 51.4% from US$0.6 million for the year ended 31 December 2010 to US$0.9 million for the year ended 31 December 2011, mainly due to the increased bank borrowings. Meanwhile, finance costs of US$0.1 million was generated from the subsidiaries newly acquired in 2011, and accounted for 8.4% of the Group's finance costs.

Taxation

Taxation increased by 45.1% from US$3.9 million for the year ended 31 December 2010 to US$5.7 million for the year ended 31 December 2011, primarily reflecting the write-down of deferred taxation arising from unrealized intra-group transaction profits in inventories at the end of the period, in accordance with International Financial Reporting Standards. At the same time, part of income tax was transferred to import tax and business tax with the change in the intra-group transaction model. Meanwhile, taxation of US$2.4 million was generated from the subsidiaries newly acquired in 2011, and accounted for 42.7% of the Group's taxation.

Profit for the Year

Profit for the year increased by 103.2% from US$30.7 million for the year ended 31 December 2010 to US$62.4 million for the year ended 31 December 2011, due to the continuous and stable growth of sales, and effective cost control. Meanwhile, profit for the year of US$13.8 million was contributed by the subsidiaries newly acquired in 2011, and accounted for 22.1% of the Group's profit for the year. Net profit margin increased by 6.4 percentage points from 23.2% for the year ended 31 December 2010 to 29.6% for the year ended 31 December 2011, as the Group benefited from economies of scale, effective cost control, and expansion of the agency promotion network.

Inventories

Inventories increased by 31.7% from US$16.0 million as at 31 December 2010 to US$21.0 million as at 31 December 2011, mainly due to the purchase associated with the increase of sales. The average inventory turnover days decreased 17 days from 91 days for the year ended 31 December 2010 to 74 days for the year ended 31 December 2011, primarily reflecting the strength of inventories management, and the shorter inventory turnover days at the subsidiaries newly acquired in 2011.

Trade Receivables

Trade receivables increased by 32.6% from US$30.4 million as at 31 December 2010 to US$40.3 million as at 31 December 2011, primarily reflecting the growth in sales. At the same time, as a result of the strengthened management on account receivables, and the majority of sales adopted cash on delivery payment terms by the subsidiaries newly acquired in 2011, the average trade receivables turnover days decreased from 71 days for the year ended 31 December 2010 to 62 days for the year ended 31 December 2011.

Trade Payables

Trade payables increased by 4,300.4% from US$0.2 million as at 31 December 2010 to US$10.7 million as at 31 December 2011, mainly due to the use of letter of credit for some of the product purchase in 2011 rather than by cash payment in 2010. The average trade payables days increased from 21 days for the year ended 31 December 2010 to 22 days for the year ended 31 December 2011.

Liquidity and Financial Resources

The following table is a summary of our consolidated statements of cash flows:

	For the year ended 31 December	
	2011	2010
	US$'000	US$'000
Net cash from operating activities	62,744	11,191
Net cash from (used in) investing activities	(107,561)	9,302
Net cash from financing activities	6,506	97,904
Net increase (decrease) in cash and cash equivalent	(38,311)	118,397
Cash and cash equivalent at beginning of the year	133,987	15,113
Effect of foreign exchange rate changes	2,230	477
Cash and cash equivalent at end of the year	97,906	133,987

Net cash from operating activities

The Group's net cash generated from operating activities was US$62.7 million for the year ended 31 December 2011, compared with US$11.2 million for the year ended 31 December 2010, an increase of 460.7%. It was mainly due to the growth of sales, the effective control on cost, and net cash flow contributed by the subsidiaries newly acquired in 2011.

Net cash from (used in) investing activities

For the year ended 31 December 2011, the Group's net cash used in investing activities was US$107.6 million, compared with net cash from investing activities of US$9.3 million for the year ended 31 December 2010, significantly decreased by 1,156.3%, mainly reflecting the prepayment for the purchase of head office, the acquisition of subsidiaries, the increase of pledged bank deposit, and the increase investment in the acquisition of product patent from acquired subsidiaries.

Net cash from financing activities

For the year ended 31 December 2011, the Group's net cash from financing activities amounted to US$6.5 million, compared with net cash from financing activities of US$97.9 million for the year ended 31 December 2010, decreased by 93.4%. It was mainly due to the proceeds from the company's global offering of shares in 2010.

Net Current Assets

	As at 31 December	
	2011	2010
	US$'000	US$'000
Current Assets		
Inventories	21,040	15,978
Trade and other receivables	73,010	49,314
Account receivables from a jointly controlled entity	-	673
Held for trading investment	-	38
Tax recoverable	95	77
Pledged bank deposit	39,471	4,530
Bank balances and cash	97,906	133,987
	231,522	204,597
Current Liabilities		
Trade and other payables	28,410	8,252
Bank borrowings-secured	39,994	4,261
Deferred consideration payables	1,147	1,198
Derivative financial instruments	645	48
Tax payable	4,088	2,709
	74,284	16,468
Net current assets	157,238	188,129

Capital Expenditures

The following table shows our capital expenditure:

	For the year ended 31 December	
	2011	2010
	US$'000	US$'000
Purchase of property, plant and equipment	13,796	832
Purchase of land use right	-	2,918
	13,796	3,750

Debts

The following table shows the Group's debts:

	As at 31 December	
	2011	2010
	US$'000	US$'000
Interest bearing bank loan and other loans	39,994	4,261

The Group's gearing ratio, calculated as bank borrowings divided by total assets, increased to 8.4% as at 31 December 2011 from 1.9% as at 31 December 2010, mainly reflecting the increase of secured bank borrowings.

Market Risks

We are exposed to various types of market risks, including changes in interest rate risks, foreign exchange risks, policy risks and inflation risks in the normal course of business. These risks are set out in the note 33 to financial statements.

Dividend

For the year ended 31 December 2011, the Group paid an interim dividend for 2011 and a final dividend for 2010 of US$10.3 million and US$15.1 million respectively. For the year ended 31 December 2010, the Group paid an interim for 2010 and a final dividend for 2009 of nil and US$4.7 million respectively.

Director and Senior Management

Executive Director

Mr. Lam Kong, aged 47, is the Chairman and Chief Executive Officer of the Group and was appointed as the Executive Director on 18 December 2006. He acquired Shenzhen Kangzhe Pharmaceutical Co., Limited through his company over 16 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 the Group's development and growth strategy and the management of the overall operation of the Group. Mr. Lam possesses clinical experience and has over 16 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 the Nomination Committee of the Company.

Mr. Chen Hongbing, aged 45, is the Chief Operating Officer of the Group and was appointed as an Executive Director on 18 December 2006. He joined the Group in 1995 and has remained with the Group since then. Mr. Chen is responsible for the operation of the Group's 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 the Group in 1995. He graduated from Nanjing Medical College with a bachelor's degree in clinical medicine in 1990.

Ms. Chen Yanling, aged 41, is the Chief Financial Officer of the Group and was appointed as an Executive Director on 18 December 2006. She joined the Group in 1995 and has remained with the Group since then. Ms. Chen is responsible for the Group's financial affairs, accountant, financing, taxation, audit, and internal control. She received her accountancy qualification in 1997 from the Ministry of Personnel of the People Republic of China and received EMBA from the International East-west University in 1999.

Mr. Hui Ki Fat, aged 70, was appointed as an Executive Director on 26 April 2007. Mr Hui has also been a Director of the Group's 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 the Mr. Hui Vincent Wing Sin, who is the Company Secretary of the Company.

Non-Executive Director

Ms. Hou Xiaoxuan, aged 45 was appointed as an Executive Director on 18 December 2006 and redesignated as a Non-executive Director on 4 June 2010. Ms. Hou joined the Group in 1995 and has remained with the 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 business. Before joining the Group, 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 49, was appointed as an Independent Non-executive Director of the Company 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 HKEx with stock code 0343) from 2000 to 2005. He 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 the Nomination Committee, a member of the Audit Committee and a member of the Remuneration Committee of the Company.

Dr. Peng Huaizheng, aged 49, was appointed as an Independent Non-executive Director of the Company 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 is a 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) 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, United Kingdom in 1998. Dr. Peng is the Chairman of the Remuneration Committee, a member of the Audit Committee and a member of the Nomination Committee of the Company.

Mr. Wu Chi Keung, aged 55, was appointed as an Independent Non-executive Director on June 25 2010. Mr. Wu has more than 30 years of experience in financial audit and specializes in providing auditing and assurance services, financial due diligence reviews, support services for merger and acquisitions, corporate restructuring and fund raising engagements. Mr. Wu was a partner of Deloitte Touche Tohmatsu until he retired in December 2008. Mr. Wu is currently the managing director of a family-owned private company engaging in property and other investment activities. He is also an Independent Non-executive Director of Jinchuan Group International Resources Co., Ltd (stock code:2362), Greater China Professional Services Limited (stock code:8193), JF Household Furnishings Limited (stock code:776), Noble Jewelry Holdings Limited (stock code:475) and China Renji Medical Group Limited (stock code:648), all the shares of which are listed on HKEx. Mr. Wu is an associate of Hong Kong Institute of Certified Public Accountants and a fellow of Association of Chartered Certified Accountants in the United Kingdom. Mr. Wu graduated from Hong Kong Polytechnic (now known as Hong Kong Polytechnic University) in 1980 with a high diploma in accountancy. Mr. Wu is the Chairman of the Audit Committee, a member of the Remuneration Committee and a member of the Nomination Committee of the Company.

SENIOR MANAGEMENT

Dr. Ma Jonathan Zheng, aged 45, has been the Chief International Operations Officer of the Group since 2007. He joined the Group as an officer responsible for the Group's international operations in 2005. He is primarily responsible for looking for and introducing new products to the 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 51, has been the Chief Technical Officer of the Group 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 the Group for selecting pharmaceutical products. Prior to this, Dr. Wong worked as manager of China pharma department for Jebsen Co. Ltd. He studied biochemistry 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 39, joined the Group and has been the Company Secretary of the Group since 2007. 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 2011.

Principal Activities

The Company is a holding company, the subsidiaries' principal activities are set out in the financial statements in note 39.

Results

The results of the Group for the year ended 31 December 2011 are set out in the consolidated statement of comprehensive income in page 41.

Reserves

Movements in reserves for the year ended 31 December 2011 are set out in the consolidated statement of changes in equity in page 44 and note 31 to the financial statements.

Distributable Reserves

As at 31 December 2011, the Group had distributable reserves of US$367.7 million available for distribution to our shareholders.

Property, Plant and Equipment

Details of changes in property, plant and equipment of the Company are set out in note 13 to the financial statements.

Share Capital

Movements in the share capital of the Company are set out in note 29 to the financial statements.

Final dividend

The Board of Directors is pleased to recommend a final dividend of US0.8 cent (equivalent to HK$0.0621) per ordinary share for the year ended 31 December 2011 to shareholders whose names appear on the Register of Members of the Company on Friday, 4 May 2012. The final dividend will be paid on Tuesday, 14 May 2012. The register of members of the Company will be closed from Wednesday, 2 May 2012 to Friday, 4 May 2012 (both days inclusive).

Bonus Issue

The Bonus Issue is proposed to be made on the basis of one (1) Bonus Share for every two (2) existing Shares held by the Shareholders whose names appear on the register of members of the Company at the close of business on the Record Date ("Bonus Issue"). The Bonus Issue will be credited as fully paid by way of capitalization of an amount in the share premium account. The Bonus Shares, upon issued, will rank pari passu in all respects with the existing Shares in issue as at the Record Date, except that they will not be entitled to the proposed cash dividend of the Company for the year ended 31 December 2011 nor will they rank for the Bonus Issue.

The Bonus Issue is conditional upon:

(i) the passing of an ordinary resolution by the Shareholders at the AGM approving the Bonus Issue; and

(ii) the Listing Committee granting the listing of, and permission to deal in, the Bonus Shares.

Set out below is a timetable for the Bonus Issue:*

	2012 :
Latest time for lodging forms of proxy for the AGM (in any event not less than 48 hours before the time appointed for holding the AGM or any adjournment thereof)	10:00 a.m.,Monday, 23 April
Date and time of the AGM	10:00 a.m., Wednesday, 25 April
Announcement of results of AGM	Wednesday, 25 April
Last day of dealings in the Shares on a cum-entitlement basis	Thursday, 26 April
First day of dealings in the Shares on an ex-entitlement basis	Friday, 27 April
Latest time for lodging transfer of Shares for registration in order to qualify for the Final Dividend and Bonus Issue	4:30 p.m.,Monday, 30 April
Closure of Register (both dates inclusive)	from Wednesday, 2 May to Friday, 4 May
Record Date for determination of entitlement to the Final Dividend and Bonus Shares	Friday, 4 May
Register re-opens	Monday, 7 May
Final Dividend and Certificates for the Bonus Shares expected to be dispatched	on or before Monday, 14 May
First day of dealings in the Bonus Shares on the Stock Exchange	Tuesday, 15 May

**Notes:*

1. *All dates and time set out in this Annual Report refer to Hong Kong dates and time.*
2. *Dates or deadlines specified in this Annual Report are indicative only and may be varied by the Company. Any consequential changes to the expected timetable will be published or notified to the Shareholders as and when appropriate and in accordance with the Listing Rules.*

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 ended 31 December 2011.

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

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. CHEN Hongbing, Mr. HUI Ki Fat and Ms. HOU Xiaoxuan 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. CHEN Hongbing, Mr. HUI Ki Fat and Ms. HOU Xiaoxuan. Details of these retiring Directors are set out in the circular issued on 22 March 2012.

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 22 to 24 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 reelection 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 38 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 2011, 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 HKEx, 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	810,146,000(L)	50.32%
			(Note 2)	
		Interest in controlled corporation	4,756,775 (L)	0.30%
			(Note 3)	
Mr. Chen Hongbing	The Company	Beneficial owner	37,358,150(L)	2.32%
		Interest in controlled corporation	50,000,000(L)	3.11%
			(Note 4)	
		Beneficial of a trust	4,756,775 (L)	0.30%
			(Note 5)	
Ms. Chen Yanling	The Company	Beneficial owner	5,223,500(L)	0.32%
		Interest in controlled corporation	2,500,000(L)	0.16%
			(Note 6)	
		Beneficial of a trust	4,756,775 (L)	0.30%
			(Note 5)	
Ms. Hou Xiaoxuan	The Company	Beneficial owner	2,000,000(L)	0.12%
		Interest in controlled corporation	50,000,000(L)	3.11%
			(Note 7)	
		Family interest	2,650,500 (L)	0.16%
			(Note 8)	
		Beneficial of a trust	4,756,775 (L)	0.30%
			(Note5)	
Mr. Hui Ki Fat	The Company	Beneficial owner	381,000(L)	0.02%
			4,720,825(L)	0.29%
			(Note9)	

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 the 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 4,756,775 Shares. The references to these 4,756,775 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. These Shares are held by Ms. Chen Yangling through Great Creation Holdings Limited, a company wholly owned by her.

7. These Shares are held by Ms. Hou Xiaoxuan through Wide Harvest Limited, a company wholly owned by her.

8. 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.

9. These Shares are held by Mr. Hui Ki Fat through Archiever Development Limited, a company wholly owned by him. Subsequent to the year ended 31 December 2011, these Shares were transferred from Archiever Development Limited to Mr. Hui Ki Fat as the beneficial owner on 9 January 2012.

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 2011, 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 the Company
APS Asset Management Pte Ltd (Note 2)	Investment manager	86,329,200 (L)	5.36%
China Fund, Inc (Note 3)	Beneficial owner	86,329,200 (L)	5.36%

Notes:

1. The letter "L" denotes Long positions in the Shares.
2. APS Asset Management Pte Ltd (APS) is a Singapore-based boutique fund management firm, and the principal activity of APS is to provide fund management, specialising in Asia Pacific equity investments, is the investment manager to the China Fund,Inc.
3. 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.

Existing Share Options

Details of the existing share options are set out in note 30 to the financial statements.

Employees

As at 31 December 2011, the Group has 1,668 employees.

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

For the year ended 31 December 2011, the percentage of sales to the Group's five largest customers was approximately 16.6% of the Group's total sales, and sales to the top customer accounted for approximately 5.0% of the total sales.

For the year ended 31 December 2011, the percentage of purchases from the Group's five largest suppliers was approximately 82.0% of the Group's total purchases, and purchase from the top supplier accounted for approximately 31.3% of the total purchases.

None of the Group's directors, the contacts of the directors, 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 33 to page 38 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 registered in the British Virgin Islands-Treasure Sea Limited ("Treasure Sea") on 14 September 2010. Mr. Lam Kong and Treasure Sea jointly undertook not to carry on businesses that are in competition with the Company's businesses.

Mr. Lam Kong and Treasure Sea stated that they complied with the relevant clauses of non-competition agreements, and did not engage into businesses that are in competition or maybe compete with the business of the Company and any of its subsidiaries, and also 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 Noncompetition with Mr. Lam Kong and Treasure Sea for the period from 1 January 2011 to 31 December 2011, 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 complied with the relevant terms of the Deed of Non-competition during the period from 1 January 2011 to 31 December 2011 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 2011.

Compliance with the Corporate Governance Code

For the year ended 31 December 2011, 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. The details of the Company's compliance with the code of Best Practice are set out on page 33 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 35 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.

Corporate Governance Report

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 year ended 31 December 2011, 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.

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.

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 for the year ended 31 December 2011.

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 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 eight 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 page 22 to page 24 of this Annual Report.

Board Attendances

During the Reporting Period, the Company held six 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 Chief Executive Officer	6/6
Mr. Chen Hongbing	Chief Operating Officer	6/6
Ms. Chen Yanling	Chief Financial Officer	6/6
Mr. Hui Ki Fat	Executive Director	5/6
Ms. Hou Xiaoxuan	Non-Executive Director	5/6
Dr. Peng Huaizheng	Independent Non-Executive Director	4/6
Mr. Wu Chi Keung	Independent Non-Executive Director	5/6
Mr. Cheung Kam Shing, Terry	Independent Non-Executive Director	4/6

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, for the year ended 31 December 2011, 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 of the Company 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

The Company 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 the 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 the Annual Report for the year ended 31 December 2011 have been reviewed by the Audit Committee, and with recommendation to the Board for approval.

For the year ended 31 December 2011, the Audit Committee has held four meetings on 24 February 2011, 20 July 2011, 15 August 2011 and 9 December 2011 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, were present at the meeting on 9 December 2011, reviewed and approved the arrangement of the annual audit work and then proposed the suggestion to the Board.

Committee Members	Attendance Rate of the Meeting for the Year Ended 31 December 2011
Mr. Wu Chi Keung	4/4
Mr. Cheung Kam Shing, Terry	4/4
Dr. Peng Huaizheng	3/4

Remuneration Committee

The Company 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 as Committee members.

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 two meetings, on 16 March 2011 and 9 December 2011, respectively. Dr. Peng Huaizheng (Chairman of the Remuneration Committee), Mr. Cheung Kam Shing, Terry, and Mr. Wu Chi Keung were present at the meeting on 16 March 2011, reviewed and approved the arrangement of remuneration for the Non-executive Directors and Executive Directors. Below is the attendance rate of the Committee members:

Committee Members	Attendance Rate of the Meeting for the Year Ended 31 December 2011
Dr. Peng Huaizheng	1/2
Mr. Cheung Kam Shing, Terry	2/2
Mr. Wu Chi Keung	2/2

Nomination Committee

The Company 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 as Committee members.

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 held two meetings on 16 March 2011 and 9 December 2011 respectively. 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 2011
Mr. Cheung Kam Shing, Terry	2/2
Mr. Lam Kong	1/2
Mr. Wu Chi Keung	2/2
Dr. Peng Huaizheng	1/2

Auditor's Remuneration

For the year ended 31 December 2011, 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$1.6 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 2011. In preparing these financial statements, the Board has selected suitable accounting policies and applied them consistently; 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.

For the year ended 31 December 2011, 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 actively communicates with shareholders and investors through multiple channels as shown below: (I) Held Annual General Meeting and Extraordinary General Meeting which provides a platform for shareholders to communicate with the board of directors of the Company (II) Timely release of the latest news and updates of the Company on the official website for the investors viewing; (III) Send information and internal magazine of the Company to shareholders and investors through e-mail or post at regular intervals.

During the year, the Company actively attended different forms of investors' communication activities, including face to face dialogue with investors, telephone conference and roadshow activities organized by sell side institutions, with the hope that investors can thoroughly understand the business model and development strategy of the Company. For the year ended 31 December 2011, Management of the Company have attended over 400 investor meetings, and received over 600 institution representatives or individual domestic and oversea investors. In addition, with the help of third party we have actively increased the interaction and communication with investors, and employed professional Hong Kong institution as consultant of investor relations, effectively maintain and improve investor relations affairs.

The Company believes that shareholders' rights should be well respected and protected. As at the date of this report, 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.

INDEPENDENT AUDITOR'S REPORT
TO THE MEMBERS OF CHINA MEDICAL SYSTEM HOLDINGS LIMITED
康哲藥業控股有限公司
(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 41 to 102, which comprise the consolidated statement of financial position as at 31 December 2011, 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 and the disclosure requirements of the Hong Kong Companies Ordinance, and for such internal control as the directors determine is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

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.

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 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 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.

INDEPENDENT AUDITOR'S REPORT

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

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 2011, 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
15 March 2012

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME
FOR THE YEAR ENDED 31 DECEMBER 2011

	NOTES	2011 US$'000	2010 US$'000
Turnover	5	210,393	132,177
Cost of goods sold		(91,272)	(54,075)
Gross profit		119,121	78,102
Other gains and losses	6	8,057	373
Selling expenses		(42,960)	(30,966)
Listing expenses		-	(2,960)
Administrative expenses		(15,339)	(9,466)
Finance costs	7	(934)	(617)
Share of result of an associate		130	112
Share of result of a jointly controlled entity		6	56
Profit before taxation		68,081	34,634
Income tax expense	9	(5,720)	(3,943)
Profit for the year	10	62,361	30,691
Other comprehensive income			
Exchange differences arising on translation		7,405	1,782
Share of other comprehensive income (expense) of an associate		2	(5)
Fair value (loss) gain on hedging instruments in cash flow hedges		(597)	97
Other comprehensive income for the year, net of income tax		6,810	1,874
Total comprehensive income for the year		69,171	32,565
Profit for the year attributable to:			
Owners of the Company		62,276	30,587
Non-controlling interests		85	104
		62,361	30,691
Total comprehensive income attributable to:			
Owners of the Company		69,037	32,461
Non-controlling interests		134	104
		69,171	32,565
		US$ cent	US$ cent
Earnings per share	12		
Basic		3.971	2.315
Diluted		3.965	2.293

CONSOLIDATED STATEMENT OF FINANCIAL POSITION
AT 31 DECEMBER 2011

	NOTES	2011 US$'000	2010 US$'000
Non-current assets			
Property, plant and equipment	13	7,724	3,282
Prepaid lease payments	14	4,533	3,142
Interest in a jointly controlled entity	15	-	99
Interest in an associate	16	1,305	1,431
Intangible assets	17	33,828	5,368
Goodwill	18	178,634	379
Deferred tax assets	19	4,688	4,431
Deposit paid for acquisition of property, plant and equipment		11,933	478
		242,645	18,610
Current assets			
Inventories	20	21,040	15,978
Trade and other receivables	21	73,010	49,314
Amount due from a jointly controlled entity	22	-	673
Held for trading investments	23	-	38
Tax recoverable		95	77
Pledged bank deposits	24	39,471	4,530
Bank balances and cash	24	97,906	133,987
		231,522	204,597
Current liabilities			
Trade and other payables	25	28,410	8,252
Bank borrowings - secured	26	39,994	4,261
Deferred consideration payables	27	1,147	1,198
Derivative financial instruments	28	645	48
Tax payable		4,088	2,709
		74,284	16,468
Net current assets		157,238	188,129
Total assets less current liabilities		399,883	206,739

	NOTES	2011	2010
		US$'000	US$'000
Capital and reserves			
Share capital	29	8,049	5,718
Reserves	31	380,564	194,271
Equity attributable to owners of the Company		388,613	199,989
Non-controlling interests		2,560	-
		391,173	199,989
Non-current liabilities			
Deferred tax liabilities	19	4,589	2,123
Deferred consideration payables	27	4,121	4,627
		8,710	6,750
		399,883	206,739

The consolidated financial statements on pages 41 to 102 were approved and authorised for issue by the Board of Directors on 15 March 2012 and are signed on its behalf by:

LAM Kong	CHEN Yanling
DIRECTOR	DIRECTOR

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY
FOR THE YEAR ENDED 31 DECEMBER 2011

	Attributable to the owners of the Company											
	Share capital US$'000	Share premium US$'000	Capital reserve US$'000 (note 31)	Share option reserve US$'000 (note 30)	Surplus reserve fund US$'000 (note 31)	Translation reserve US$'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 2010	4,741	6,079	4,911	570	8,159	6,555	(145)	18,122	4,741	53,733	201	53,934
Profit for the year	-	-	-	-	-	-	-	30,587	-	30,587	104	30,691
Other comprehensive income for the year	-	-	-	-	-	1,777	97	-	-	1,874	-	1,874
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 29)	850	110,030	-	-	-	-	-	-	-	110,880	-	110,880
Issue of new shares for cash under over-allotment option (note 29)	100	12,945	-	-	-	-	-	-	-	13,045	-	13,045
Issue costs of new shares	-	(4,965)	-	-	-	-	-	-	-	(4,965)	-	(4,965)
Deemed distribution to shareholders	-	-	(632)	-	-	-	-	-	-	(632)	-	(632)
Acquisition of additional interest in a subsidiary	-	-	(2,221)	-	-	-	-	-	-	(2,221)	(104)	(2,325)
Dividends paid to a non-controlling shareholders	-	-	-	-	-	-	-	-	-	-	(201)	(201)
Dividends paid	-	-	-	-	-	-	-	-	(4,741)	(4,741)	-	(4,741)
Dividend 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
Profit for the year	-	-	-	-	-	-	-	62,276	-	62,276	85	62,361
Other comprehensive income for the year	-	-	-	-	-	7,358	(597)	-	-	6,761	49	6,810
Total comprehensive income for the year	-	-	-	-	-	7,358	(597)	62,276	-	69,037	134	69,171
Issue of shares for exercise of share options (note 29)	71	1,518	-	-	-	-	-	-	-	1,589	-	1,589
Issue of shares in consideration for the acquisition of a subsidiary (note 29 and note 34(a))	650	142,703	-	-	-	-	-	-	-	143,353	-	143,353
Transfer of share option reserve on exercise of share option	-	570	-	(570)	-	-	-	-	-	-	-	-
Release of translation reserve upon disposal of a jointly controlled entity	-	-	-	-	-	(5)	-	5	-	-	-	-
Acquisition of a subsidiary (note 34(b))	-	-	-	-	-	-	-	-	-	-	2,426	2,426
Dividends paid	-	-	-	-	-	-	-	(10,487)	(14,868)	(25,355)	-	(25,355)
Dividends proposed	-	-	-	-	-	-	-	(12,879)	12,879	-	-	-
Bonus issue (note 29)	1,610	(1,610)	-	-	-	-	-	-	-	-	-	-
Transfer of reserves	-	-	-	-	2,341	-	-	(2,341)	-	-	-	-
Balance at 31 December 2011	8,049	269,672	2,058	-	11,499	15,685	(645)	69,416	12,879	388,613	2,560	391,173

CONSOLIDATED STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED 31 DECEMBER 2011

	NOTES	2011 US$'000	2010 US$'000
Operating activities			
Profit before taxation		68,081	34,634
Adjustments for:			
Share of result of an associate		(130)	(112)
Share of result of a jointly controlled entity		(6)	(56)
Amortisation of intangible assets	17	3,087	839
Depreciation of property, plant and equipment	13	1,072	724
Release of prepaid lease payments		90	67
Interest income		(2,265)	(505)
Interest expenses		673	327
Imputed interest expense on deferred consideration payables		261	290
Listing expenses		-	2,960
Gain on disposal of property, plant and equipment		(8)	(1)
Loss on disposal of a jointly controlled entity		20	-
Allowance for inventories		55	222
Allowance for bad and doubtful debts		107	18
Operating cash flows before movements in working capital		71,037	39,407
Increase in inventories		(1,546)	(4,797)
Increase in trade and other receivables		(13,200)	(15,224)
Decrease (increase) in held for trading investments		38	(7)
Decrease (increase) in amount due from a jointly controlled entity		673	(192)
Increase (decrease) in trade and other payables		11,083	(2,802)
Cash generated from operations		68,085	16,385
PRC Enterprise Income Tax paid		(5,042)	(5,068)
Hong Kong Profits Tax paid		(299)	(126)
Net cash from operating activities		62,744	11,191
Investing activities			
Purchase of property, plant and equipment		(13,796)	(832)
Purchase of land use right		-	(2,918)
Repayment of deferred consideration payables	34(a)	(11,455)	-
Repayment of deferred consideration payables - others		(1,105)	(774)
Placement of pledged bank deposit		(38,488)	(4,530)
Release of pledged bank deposit		4,643	17,641
Interest received		2,265	505
Dividend received from an associate		258	183
Proceeds from disposal of property, plant and equipment		36	27
Proceeds from disposal of a jointly controlled entity		85	-
Acquisition of subsidiaries	34	(50,004)	-
Net cash (used in) from investing activities		(107,561)	9,302

	2011 US$'000	2010 US$'000
Financing activities		
Interest paid	(918)	(370)
Dividends paid	(25,355)	(4,741)
Proceeds from issue of shares	1,589	124,029
New bank borrowings raised	39,970	4,261
Expenses incurred in connection with listing of shares to Main Board	-	(8,557)
Repayment of borrowings	(8,780)	(16,517)
Dividends paid to non-controlling shareholders	-	(201)
Net cash from financing activities	6,506	97,904
Net (decrease) increase in cash and cash equivalents	(38,311)	118,397
Cash and cash equivalent at 1 January	133,987	15,113
Effect of foreign exchange rate changes	2,230	477
Cash and cash equivalent at 31 December represented by bank balances and cash	97,906	133,987

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2011

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 an 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 International Accounting Standards ("IAS"s), IFRSs, amendment and interpretations ("INT"s) (hereinafter collectively referred to as "new and revised IFRSs") issued by the International Accounting Standards Board (the "IASB") and IFRS Interpretations Committee (the "IFRIC") of the IASB.

Amendments to IFRSs	Improvements to IFRSs issued in 2010
IAS 24 (as revised in 2009)	Related party disclosures
Amendments to IAS 32	Classification of rights issues
Amendments to IFRIC - INT 14	Prepayments of a minimum funding requirement
IFRIC - INT 19	Extinguishing financial liabilities with equity instruments

Except as described below, the application of the new and revised IFRSs in the current year has had no material impact on the Group's financial performance and positions for the current and prior years and/or on the disclosures set out in these consolidated financial statements.

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

<u>Amendments to IAS 1 Presentation of financial statements (as part of Improvements to IFRSs issued in 2010)</u>

The amendments to IAS 1 clarify that an entity may choose to disclose an analysis of other comprehensive income by item in the consolidated statement of changes in equity or in the notes to the consolidated financial statements. In the current year, for each component of equity, the Group has chosen to present such an analysis in the consolidated statement of comprehensive income with a single-line presentation of other comprehensive income in the consolidated statement of changes in equity. Such amendments have been applied retrospectively, and hence the disclosures in these consolidated financial statements have been modified to reflect the change.

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

Amendments to IFRS 7	Disclosures - Transfers of financial assets[1]
	Disclosures - Offsetting financial assets and financial liabilities[2]
	Mandatory effective date of IFRS 9 and transition disclosures[3]
IFRS 9	Financial instruments[3]
IFRS 10	Consolidated financial statements[2]
IFRS 11	Joint arrangements[2]
IFRS 12	Disclosure of interests in other entities[2]
IFRS 13	Fair value measurement[2]
Amendments to IAS 1	Presentation of items of other comprehensive income[5]
Amendments to IAS 12	Deferred tax - Recovery of underlying assets[4]
IAS 19 (as revised in 2011)	Employee benefits[2]
IAS 27 (as revised in 2011)	Separate financial statements[2]
IAS 28 (as revised in 2011)	Investments in associates and joint ventures[2]
Amendments to IAS 32	Offsetting financial assets and financial liabilities[6]
IFRIC - INT 20	Stripping costs in the production phase of a surface mine[2]

[1] Effective for annual periods beginning on or after 1 July 2011.
[2] Effective for annual periods beginning on or after 1 January 2013.
[3] Effective for annual periods beginning on or after 1 January 2015.
[4] Effective for annual periods beginning on or after 1 January 2012.
[5] Effective for annual periods beginning on or after 1 July 2012.
[6] Effective for annual periods beginning on or after 1 January 2014.

The directors of the Company anticipate that the adoption of these standards will have no material impact on the Group's result 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 of Hong Kong Limited and by the Hong Kong Companies Ordinance.

The consolidated financial statements have been prepared on the historical cost basis, except for certain financial instruments that are measured at fair value, as explained in the accounting policies set out below. Historical cost is generally based on the fair value of the consideration given in exchange of goods.

<u>Basis of consolidation</u>

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 (effective from 1 January 2010 onwards).

Changes in the Group's ownership interests in existing subsidiaries

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. The fair value of the shares issued by the Company in consideration for the acquisition of equity interest in a subsidiary is determined based on the fair value of the shares at the time when changes in ownership interests take place.

3. SIGNIFICANT ACCOUNTING POLICIES - continued

Business combinations

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.

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-based payment arrangements of the acquiree or share-based payment arrangements of the Group entered into to replace share-based payment arrangements of the acquiree 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, when applicable, on the basis specified in another Standard.

If the initial accounting for a business combination is incomplete by the end of the reporting period in which the combination occurs, the Group reports provisional amounts for the items for which the accounting is incomplete. Those provisional amounts are adjusted during the measurement period (see above), or additional assets or liabilities are recognised, to reflect new information obtained about facts and circumstances that existed as of the acquisition date that, if known, would have affected the amounts recognised as of that date.

3. SIGNIFICANT ACCOUNTING POLICIES - continued

Goodwill

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

For the purposes of impairment testing, goodwill is allocated to each of the cash-generating units (or groups of cash-generating units) that is expected to benefit from the synergies of the combination.

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 Group 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 initially recognised in the consolidated statement of financial position at cost and adjusted thereafter to recognise the Group's share of the profit or loss and other comprehensive income of the associates. 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.

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.

3. SIGNIFICANT ACCOUNTING POLICIES - continued

Investment in an associate - continued

The requirements of IAS 39 are applied to determine whether it is necessary to recognise any impairment loss with respect to the Group's investment in an associate. When necessary, the entire carrying amount of the investment (including goodwill) is tested for impairment in accordance with IAS 36 "Impairment of assets" as a single asset by comparing its recoverable amount (higher of value in use and fair value less costs to sell) with its carrying amount. Any impairment loss recognised forms part of the carrying amount of the investment. Any reversal of that impairment loss is recognised in accordance with IAS 36 to the extent that the recoverable amount of the investment subsequently increases.

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.

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, investments in jointly controlled entities are initially recognised in the consolidated statement of financial position at cost and adjusted thereafter to recognise the Group's share of the profit or loss and other comprehensive income of the jointly controlled entities. 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.

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.

Upon disposal of a jointly controlled entity that results in the Group losing joint control over that jointly controlled entity, any retained investment is measured at fair value at that date and the fair value is regarded as its fair value on initial recognition as a financial asset in accordance with IAS 39. The difference between the previous carrying amount of the jointly controlled entity attributable to the retained interest and its fair value is included in the determination of the gain or loss on disposal of the jointly controlled entity. In addition, the Group accounts for all amounts previously recognised in other comprehensive income in relation to that jointly controlled entity on the same basis as would be required if that jointly controlled entity had directly disposed of the related assets or liabilities. Therefore, if a gain or loss previously recognised in other comprehensive income by that jointly controlled entity would be reclassified to profit or loss on the disposal of the related assets or liabilities, the Group reclassifies the gain or loss from equity to profit or loss (as a reclassification adjustment) when it loses joint control over 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's 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

<u>Intangible assets</u>

Intangible assets acquired separately

Intangible assets acquired separately and with finite useful lives are carried at costs 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. The estimated useful life and amortisation method are reviewed at the end of each reporting period, with the effective of any changes in estimate being accounted for on a prospective basis. Intangible assets with indefinite useful lives that are acquired separately are carried at cost less any subsequent accumulated impairment losses (see the accounting policy in respect of impairment losses on tangible and intangible assets below).

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 activities (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. Subsequent to initial recognition, internally-generated intangible asset is measured at cost less accumulated amortisation and accumulated impairment losses (if any), on the same basis as intangible assets acquired separately.

<u>Intangible assets acquired in a business combination</u>

Intangible assets acquired in a business combination are recognised separately from goodwill and are initially recognised at their fair value at the acquisition date (which is regarded as their cost).

Subsequent to initial recognition, intangible assets with finite useful lives are carried at costs 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. Alternatively, intangible assets with indefinite useful lives are carried at cost less any subsequent accumulated impairment losses (see the accounting policy in respect of impairment losses on tangible and intangible assets below).

3. SIGNIFICANT ACCOUNTING POLICIES - continued

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 in the consolidated statement of financial position at cost less subsequent accumulated depreciation and accumulated impairment losses, if any.

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.

Impairment losses on tangible and intangible assets other than goodwill

At the end of the 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 any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss, if any. When it is not possible to estimate the recoverable amount of an individual asset, the Group estimates the recoverable amount of the cash-generating unit to which the asset belongs. Where a reasonable and consistent basis of allocation can be identified, corporate assets are also allocated to individual cash-generating units, or otherwise they are allocated to the smallest group of cash-generating units for which a reasonable and consistent allocation basis can be identified.

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

If the recoverable amount of an asset is estimated to be less than its carrying amount, the carrying amount of the asset (or a cash-generating unit) is reduced to its recoverable amount. An impairment loss is recognised immediately in profit or loss.

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 years. A reversal of an impairment loss is recognised as income immediately.

3. SIGNIFICANT ACCOUNTING POLICIES - continued

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.

Financial assets

The Group's financial assets are classified into financial assets held for trading and loans and receivables. The classification depends on the nature and purpose of the financial assets and is determined at the time of initial recognition. 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.

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.

3. SIGNIFICANT ACCOUNTING POLICIES - continued

Financial instruments - continued

Financial assets - continued

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.

Financial assets held for trading at fair value are measured at fair value, with changes in fair value arising from remeasurement 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 is included in the 'other gains and losses' line item in the consolidated statement of comprehensive income.

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 considered to be 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 and other receivables that are assessed not to be impaired individually are, in addition, 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.

3. SIGNIFICANT ACCOUNTING POLICIES - continued

Financial instruments - continued

Financial assets - continued

Impairment of financial assets - continued

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

The carrying amount of the financial asset is reduced by the impairment loss directly for all financial assets with the exception of trade 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 instruments

Financial liabilities and equity instruments issued by a group entity are classified as either financial liabilities or as equity in accordance with the substance of the contractual arrangements 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 (including all fees and points paid or received that form an integral part of the effective interest rate, transaction costs and other premiums or discounts) through the expected life of the financial liability, or, where appropriate, a shorter period, to the net carrying amount on initial recognition.

Interest expense is recognised on an effective interest basis.

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

Financial liabilities and equity 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 when 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 and accumulated in hedging reserve. The gain or loss relating to the ineffective portion 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, in the same line of the consolidated statement of comprehensive income as the recognised hedged item.

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

The Group derecognises a financial asset only when the contractual rights to the cash flows from the asset expire, or when it transfers the financial asset and substantially all the risks and rewards of ownership of the asset to another entity. If the Group neither transfers nor retains substantially all the risks and rewards of ownership and continues to control the transferred asset, the Group continues to recognise the asset to the extent of its continuing involvement and recognises an associated liability. If the Group retains substantially all the risks and rewards of ownership of a transferred financial asset, the Group continues to recognise the financial asset and also recognises a collateralised borrowing for the proceeds received.

On derecognition of a financial asset in its entirety, the difference between the asset's carrying amount and the sum of the consideration received and receivable and the cumulative gain or loss that had been recognised in other comprehensive income and accumulated in equity is recognised in profit or loss.

The Group derecognises a financial liability when, and only when, the Group's obligations are discharged, cancelled or expire. The difference between the carrying amount of the financial liability derecognised and the consideration paid and payable is recognised in profit or loss.

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 recognised when it is probable that the economic benefits will flow to the Group and the amount of income can be measured reliably. Interest income 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.

3. SIGNIFICANT ACCOUNTING POLICIES - continued

Taxation

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

The tax currently payable is based on taxable profit for the year. Taxable profit differs from profit as reported in the consolidated 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. Deferred tax assets are generally recognised for all deductible temporary difference to the extent that it is probable that taxable profit will be available against which those 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.

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 is 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 asset 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.

Current and 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 current and deferred tax are also recognised in other comprehensive income or directly in equity respectively.

Whether current tax or deferred tax arises from the initial accounting for a business combination, the tax effect is included in the accounting for the business combination.

3. SIGNIFICANT ACCOUNTING POLICIES - continued

Foreign currencies

Where current tax or deferred tax arises from the initial accounting for a business combination, the tax effect is included in the accounting for the business combination.

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 year in which they arise.

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$) using exchange rate prevailing at the end of the reporting period. Income and expenses items 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 under the heading of translation reserve.

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.

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, unless it is clear that both elements are operating leases in which case the entire lease is classified as an operating lease. 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

All borrowing costs are recognised in profit or loss in the period in which they are incurred.

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.

Retirement benefit costs

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

3. SIGNIFICANT ACCOUNTING POLICIES - continued

Equity-settled share-based payment transactions

Share options granted to employees

A shareholder of the Company has granted shares of the Company 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 as 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 accumulated profits.

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 year, that have a significant risk of causing a material adjustment to the carrying amount of assets and liabilities, are described below.

Impairment of goodwill and intangible assets

For the purpose of impairment testing, the entire amount of goodwill and part of the intangible assets have been allocated to the three cash generating unites ("CGU"s) (see note 18). The impairment assessment is based on the value in use of the CGUs. The value in use of the related CGUs requires the Group to estimate the expected future cash flows from the Group's exclusive distribution rights, agency right and patent rights. If the actual future cash flows are less than expected, impairment may be required. In the opinion of the directors of the Company, no impairment is required for the year ended 31 December 2011 and 2010.

4. KEY SOURCES OF ESTIMATION UNCERTAINTY - continued

Impairment of property, plant and equipment

The impairment of the property, plant and equipment is based on the valuation of the recoverable amount with reference to expected future cash flows on management's estimation. Value in use of the related cash-generating units 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, impairment may be required. The carrying amount of the property, plant and equipment as at 31 December 2011 is US$7,724,000 (2010: US$3,282,000) (see note 13).

Deferred tax assets

As at 31 December 2011, a deferred tax asset of US$4,688,000 (2010: US$4,431,000) 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.

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 were deteriorated, resulting in an impairment of their ability to make payments, additional impairment may be required. As at 31 December 2011, the carrying amounts of trade receivables (net of allowance for bad and doubtful debts) and allowance for bad and doubtful debts are US$40,305,000 (2010: US$30,394,000) and US$331,000 (2010: US$215,000) 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.

In the current year, the Group changed its internal reporting structure such that it only has one reportable operating segment, that is marketing, promotion, sales and manufacturing of pharmaceutical products whilst in previous years, the Group had two reportable operating segments, including (a) marketing, promotion and sales of pharmaceutical products and (b) others. However, other than revenue analysis that is disclosed below, no operating results and other discrete financial information is available for the assessment of performance of the respective business divisions. In additional, the operation regarding the manufacturing of the pharmaceutical products is not material to the Group and hence the directors of the Company consider it with other operations for performance assessment and resources allocation purpose.

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.

The Group primarily operates in the PRC. All revenue for external customers are attributed to the PRC and a majority of 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:

	2011 US$'000	2010 US$'000
Deanxit	67,046	52,341
Ursofalk	46,244	35,879
Nesiritide	18,352	12,576
Yinuoshu	16,269	-
Shaduolika	15,657	-
Exacin	10,505	10,632
Augentropfen Stulln Mono eye-drops	9,800	8,445
Salofalk	7,084	3,989
GanFuLe	4,874	4,219
Bioflor	4,863	1,266
Protein Hydrolysate	1,142	-
Cystistat	1,106	738
Others	7,451	2,092
Total	210,393	132,177

6. OTHER GAINS AND LOSSES

	2011 US$'000	2010 US$'000
Net exchange gain (loss)	4,283	(729)
Government subsidies (Note)	1,245	391
Interest income	2,265	505
Loss on disposal of a jointly controlled entity	(20)	-
Fair value change on investments held for trading	42	172
Gain on disposal of property, plant and equipment	8	1
Others	234	33
	8,057	373

Note: During the year ended 31 December 2011, a subsidiary the Group received a refund of value-added tax on sales from the relevant PRC tax authority to encourage business in the PRC. In addition, incentive subsidies are provided by the PRC local authorities to the Group to reimburse the research and development expenses incurred in prior years. There were no unfulfilled conditions attached to these grants and, the Group has recognised the grants upon receipts.

7. FINANCE COSTS

	2011 US$'000	2010 US$'000
Interest on bank borrowings wholly repayable within five years	673	327
Imputed interest on deferred consideration payables	261	290
	934	617

8. DIRECTORS' AND EMPLOYEES' EMOLUMENTS

	2011 US$'000	2010 US$'000
Directors' fees	184	186
Other emoluments to executive directors		
- basic salaries and allowances	316	309
- retirement benefits scheme contributions	16	13
	516	508

8. DIRECTORS' AND EMPLOYEES' EMOLUMENTS - continued

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

	2011 US$'000	2010 US$'000
Mr. Lam Kong		
- directors' fee	23	23
- basic salaries and allowances	93	93
- retirement benefits scheme contributions	2	2
	118	118
Mr. Chen Hong Bing		
- directors' fee	23	23
- basic salaries and allowances	98	94
- retirement benefits scheme contributions	4	3
	125	120
Ms. Hou Xiao Xuan		
- directors' fee	23	23
- basic salaries and allowances	-	-
- retirement benefits scheme contributions	6	5
	29	28
Ms. Chen Yan Ling		
- directors' fee	23	23
- basic salaries and allowances	79	75
- retirement benefits scheme contributions	4	4
	106	102
Mr. Hui Ki Fat		
- directors' fee	23	23
- basic salaries and allowances	46	46
- retirement benefits scheme contributions	-	-
	69	69
Mr. Paul Bernard Harper		
- directors' fee	-	8
- basic salaries and allowances	-	-
- retirement benefits scheme contributions	-	-
	-	8
Mr. Stuart Hamilton Leckie		
- directors' fee	-	27
- basic salaries and allowances	-	-
- retirement benefits scheme contributions	-	-
	-	27

8. DIRECTORS' AND EMPLOYEES' EMOLUMENTS - continued

	2011 US$'000	2010 US$'000
Mr. Peng Huaizheng		
- directors' fee	23	15
- basic salaries and allowances	-	-
- retirement benefits scheme contributions	-	-
	23	15
Mr. Wu Chi Keung		
- directors' fee	23	12
- basic salaries and allowances	-	-
- retirement benefits scheme contributions	-	-
	23	12
Mr. Cheung Kam Shing, Terry		
- directors' fee	23	9
- basic salaries and allowances	-	-
- retirement benefits scheme contributions	-	-
	23	9
Total	516	508

The five highest paid individuals for the year ended 31 December 2010 and 2011 included three directors for both years, details of whose emoluments are set out above. The emoluments of the remaining individuals for the years were as follows:

	2011 US$'000	2010 US$'000
Employees		
- basic salaries and allowances	158	146
- retirement benefits scheme contributions	4	3
	162	149

The emoluments of the employee were within the following bands:

	Number of employees 2011	Number of employees 2010
Up to HK$1,000,000	2	2

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. INCOME TAX EXPENSE

	2011 US$'000	2010 US$'000
Current tax:		
PRC Enterprise Income Tax	5,599	6,397
Hong Kong Profits Tax	595	187
Other jurisdictions	6	6
	6,200	6,590
(Over)underprovision in prior years		
PRC Enterprise Income Tax	(179)	(11)
Hong Kong Profits Tax	8	-
	(171)	(11)
Deferred taxation (note 19):		
- Current year	(309)	(2,636)
Taxation charge for the year	5,720	3,943

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 2011, the Enterprise Income Tax rate applicable to 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 22% to 24% (2010: 20% to 22%).

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") and 常德康哲醫藥有限公司 (Changde Kangzhe Pharmaceutical Co., Ltd.) ("Kangzhe Changde") are entitled to a tax reduction to 15% granted by the local tax authority and such tax concession are subject to renewal by the relevant tax bureau annually.

During the year, the Group newly acquired two subsidiaries, 天津康哲醫藥科技發展有限公司 (Tianjin Kangzhe Pharmaceutical Technology Development Co., Limited) (formerly known as 天津普瑞森醫藥貿易有限公司) ("Kangzhe Tianjin") (see note 34(a)) and 廣西康哲廣明藥業有限公司 (Guangxi Kangzhe Guangming Pharmaceutical Co., Limited) (formerly known as 廣西廣明藥業有限公司) ("Kangzhe Guangming") (see note 34(b)). Kangzhe Tianjin is entitled to a tax reduction to 15% for 3 years, starting from 1 January 2009, granted by the local tax authority. Kangzhe Guangming is entitled to a tax reduction of 15% for 10 years, starting from 1 January 2011.

9. INCOME TAX EXPENSE - 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 2011 and 2010, 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:

	2011 US$'000	2010 US$'000
Profit before taxation	68,081	34,634
Tax at the applicable tax rate (Note)	16,339	7,619
Tax effect of share of result of a jointly controlled entity	(2)	(12)
Tax effect of share of results of associates	(31)	(25)
Tax effect of expenses that are not deductible in determining taxable profit	1,088	1,162
Tax effect of income that is not taxable in determining taxable profit	(669)	(59)
Tax effect of tax losses not recognised	56	83
Tax effect of tax concession	(2,293)	(11)
Effect on different applicable tax rates of subsidiaries	(436)	(457)
Effect of tax benefit arising from Labuan Tax Act	(8,193)	(4,718)
Overprovision in prior years	(171)	(11)
Utilisation of tax loss previously not recognised	(24)	(11)
Deferred tax arising from withholding tax on undistributed profit of a PRC subsidiary	191	359
Others	(135)	24
Taxation charge for the year	5,720	3,943

Note: The applicable PRC Enterprise Income Tax rate of 24% (2010: 22%) is the prevailing tax rate in Shenzhen, the PRC, where the operations of the Group are substantially based and the taxation charge mainly represents the income tax of Kangzhe Shenzhen.

10. PROFIT FOR THE YEAR

	2011 US$'000	2010 US$'000
Profit for the year has been arrived at after charging:		
Directors' remuneration		
Fees	184	186
Other emoluments	316	309
Pension costs	16	13
	516	508
Other staff costs	17,717	13,501
Pension costs	987	777
Key employee benefit expense (note 38)	153	104
Total staff costs	19,373	14,890
Auditor's remuneration	268	165
Allowance for bad and doubtful debts	107	18
Allowance for inventories	55	222
Release of prepaid lease payments	90	67
Depreciation of property, plant and equipment	1,072	724
Amortisation of intangible assets (included in cost of goods sold)	3,087	839
Cost of inventories recognised as an expense	88,059	52,821
Minimum lease payment under operating lease in respect of property	833	620

11. DIVIDENDS

	2011 US$'000	2010 US$'000
Dividend paid		
Final dividend in respect of the year ended 31 December 2010 of US$0.013 (year ended 31 December 2009: US$0.10) per share on 1,157,865,340 (2009:47,408,904) shares	15,054	4,741
Interim dividend in respect of the six months ended 30 June 2011 of US$0.008 per share on 1,287,865,340	10,301	-
	25,355	4,741
Dividend proposed		
Proposed final dividend in respect of the year ended 31 December 2011 of US$0.008 (in respect of the year ended 31 December 2010: US$0.013) per share of par value of US$0.005 (2010: US$0.005) on 1,609,831,000 (2010: 1,143,691,000) shares	12,879	14,868

The Board of Directors have declared a final dividend of US$0.008 per ordinary share of par value of US$0.005 for the year ended 31 December 2011 (2010: US$0.013 per ordinary share of par value of US$0.005).

12. 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:

	2011	2010
	US$'000	US$'000
Earnings for the purposes of basic and diluted earnings per share (profit attributable to owners of the Company)	62,276	30,587

	Number of ordinary shares As at 31 December	
	2011	2010
Weighted average number of ordinary shares for the purpose of basic earnings per share	1,568,446,805	1,321,385,445
Effect of dilutive potential ordinary shares on share options	2,259,466	12,607,889
Weighted average number of ordinary shares for the purpose of diluted earnings per share	1,570,706,271	1,333,993,334

The number of shares for the purpose of calculating basic and diluted earnings per share for the year ended 31 December 2010 have been adjusted to reflect the share sub-division (see note 29) effective in June 2010.

The number of shares for the purpose of calculating basic and diluted earnings per share has been adjusted to reflect the bonus issue (see note 29) effective on September 2011.

13. 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 2010	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
Currency realignment	201	10	177	118	69	19	594
Acquired on acquisition of subsidiaries	1,948	-	816	23	71	53	2,911
Additions	-	-	230	1,337	219	555	2,341
Disposals	-	-	-	(66)	(19)	-	(85)
Transfer	20	-	-	-	-	(20)	-
At 31 December 2011	4,899	205	4,050	3,109	1,583	683	14,529
DEPRECIATION							
At 1 January 2010	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
Currency realignment	74	10	121	53	46	-	304
Provided for the year	208	-	250	438	176	-	1,072
Eliminated on disposals	-	-	-	(42)	(15)	-	(57)
At 31 December 2011	1,618	205	2,643	1,295	1,044	-	6,805
CARRYING VALUES							
At 31 December 2011	3,281	-	1,407	1,814	539	683	7,724
At 31 December 2010	1,394	-	555	851	406	76	3,282

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

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

14. PREPAID LEASE PAYMENTS

	2011	2010
	US$'000	US$'000
The Group's prepaid lease payments comprise:		
Leasehold land in the PRC:		
Medium-term leases	4,612	3,210
Analysed for reporting purposes as:		
Current asset (included in trade and other receivables)	79	68
Non-current asset	4,533	3,142
	4,612	3,210

15. INTEREST IN A JOINTLY CONTROLLED ENTITY

	2011	2010
	US$'000	US$'000
Cost of unlisted investment in a jointly controlled entity	-	-
Share of post-acquisition profits and other comprehensive income	-	99
	-	99

As at 31 December 2011 and 2010, the details of the jointly controlled entity are as follows:

Name of jointly controlled entity	Place of establishment and business	Attributable equity interest held by the Group 2011	Attributable equity interest held by the Group 2010	Principal activity
廣東蘭太康虹醫藥有限公司 (Guangdong Lan Tai Kanghong Pharmaceutical Ltd.) ("Guangdong Lantai")	PRC	- (note)	55%	Distribution of medicine

Note: During the year ended 31 December 2011, the jointly controlled entity was disposed of to a third party for a consideration of RMB561,000 (approximately US$85,000) and loss on disposal of US$20,000 was recognised in profit or loss.

15. INTEREST IN A JOINTLY CONTROLLED ENTITY - continued

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

	2011	2010
	US$'000	US$'000
Total assets	-	1,106
Total liabilities	-	925
Net assets	-	181
Group's share of net assets of a jointly controlled entity	-	99

	2011	2010
	US$'000 (note)	US$'000
Turnover	334	1,419
Profit for the year	11	98
Group's share of result of a jointly controlled entity	6	56

Note: The financial information is up to the Group's jointly controlled entity disposal day.

16. INTEREST IN AN ASSOCIATE

	2011	2010
	US$'000	US$'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	(382)	(256)
	1,305	1,431

As at 31 December 2011 and 2010, the details of the associate are as follows:

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

16. INTEREST IN AN ASSOCIATE - continued

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

	2011 US$'000	2010 US$'000
Total assets	5,329	5,844
Total liabilities	2	1
Net assets	5,327	5,843
Group's share of net assets of an associate	1,305	1,431

	2011 US$'000	2010 US$'000
Turnover	535	462
Profit for the year	531	457
Other comprehensive expense	(8)	(20)
Group's share of result of an associate for the year	130	112
Group's share of other comprehensive income (expense) of an associate	2	(5)

17. INTANGIBLE ASSETS

	Exclusive distribution rights US$'000 (Note a(i))	Exclusive agency right US$'000 (Note b)	Patent rights US$'000	Total US$'000
COST				
At 1 January 2010	952	7,403	-	8,355
Exchange adjustments	25	-	-	25
Adjustment (note a(ii))	(261)	-	-	(261)
At 31 December 2010	716	7,403	-	8,119
Exchange adjustments	308	-	942	1,250
Acquired on acquisition of subsidiaries (note c)	6,896	-	23,498	30,394
At 31 December 2011	7,920	7,403	24,440	39,763
AMORTISATION				
At 1 January 2010	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
Exchange adjustments	70	-	27	97
Charge for the year	1,272	740	1,075	3,087
At 31 December 2011	2,041	2,792	1,102	5,935
CARRYING VALUES				
At 31 December 2011	5,879	4,611	23,338	33,828
At 31 December 2010	17	5,351	-	5,368

(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 西藏諾迪康藥業股份有限公司 (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).

17. INTANGIBLE ASSETS - continued

(a) Exclusive distribution right - continued

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.

As at 31 December 2011, the exclusive distribution right has been fully amortised during the year.

(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 of US$224,000 for the year ended 31 December 2010.

(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 27) 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.

17. INTANGIBLE ASSETS - continued

(c) Acquisition of exclusive distribution rights and patent rights

The Group acquired 100% of equity interest in Great Move Enterprises Limited ("Great Move") and 51% of equity interest in Kangzhe Guangming on 3 April 2011 and 30 April 2011 respectively. This included the acquisition of exclusive distribution rights and patent rights for the sales of several products. The exclusive distribution rights and patent rights were measured at their fair values at the date of acquisition and the valuation of the intangible assets is performed by Vigers Appraisal & Consulting Limited, an independent valuer.

The fair value of the patent rights is determined based on the royalty rate method by capitalising future royalty income which a market participant would be willing to pay to use the patents for the remaining term of the patent right. The fair value of the exclusive distribution rights is determined based on the multi-period excess earnings method by capitalising future cashflows derived from the intangible assets for the remaining term of the distribution rights.

As at the acquisition date, the major patent rights owned by Kangzhe Tianjin, the wholly owned subsidiary of Great Move, represented Yinoushu and Shaduolika amounting to US$21,035,000 and US$1,264,000 respectively and the exclusive distribution right and patent right of Protein Hydrolystate owned by Kangzhe Guangming amounting to US$894,000 and US$1,199,000 respectively.

The exclusive distribution rights and patent rights of Kangzhe Tianjin and Kangzhe Guangming will expire from 31 December 2011 to 7 May 2028.

18. GOODWILL

	US$'000
At 1 January 2010 and 31 December 2010	379
Arising on acquisition of subsidiaries (note 34)	178,255
At 31 December 2011	178,634

For the purposes of impairment testing, the entire amount of goodwill has been allocated to three CGUs, representing three subsidiaries, namely Kangzhe Tianjin, Kangzhe Guangming and Sky United Trading Limited ("Sky United"). Kangzhe Tianjin and Sky United are engaged in trading of drugs. Kangzhe Guangming is engaged in production of medicines. The relevant intangible assets are allocated to the CGUs. The carrying amounts of goodwill and intangible assets as at 31 December 2011 allocated to these units are as follows:

	Goodwill		Intangible assets	
	2011	2010	2011	2010
	US$'000	US$'000	US$'000	US$'000
Kangzhe Tianjin	176,978	-	27,173	-
Kangzhe Guangming	1,277	-	2,044	-
Sky United	379	379	-	-
	178,634	379	29,217	-

18. GOODWILL - continued

The recoverable amounts of the CGUs are determined based on 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 CGUs. 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.

Kangzhe Tianjin

At 31 December 2011, the impairment review is determined based on cash flow projections which was derived from the financial budgets approved by management covering a three-year period, and discount rate of 10%. Kangzhe Tianjin's cash flows beyond the third-year period are extrapolated using a steady growth rate ranging from 0% to 8%. This growth rate is based on the relevant industry growth forecasts and does not exceed the average long-term growth rate for the relevant industry.

Kangzhe Guangming

At 31 December 2011, the impairment review is determined based on cash flow projections which was derived from the financial budgets approved by management covering a three-year period, and discount rate of 10%. For impairment review purpose, the cash flow projection was extrapolated for ten years based on the assumption that a growth rate of 10% is expected after the third year. This growth rate is based on the relevant industry growth forecasts and does not exceed the average long-term growth rate for the relevant industry. Due to the synergetic effect from business combination, management of the Group believes that the growth rate is reasonable.

19. 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	Fair value adjustments to intangible assets acquired in business combinations US$'000	Others (note) US$'000	Total US$'000
At 1 January 2010	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
Acquisitions	-	-	(2,433)	-	(2,433)
Credit (charge) to profit or loss for the year (note 9)	268	(191)	248	(16)	309
Exchange differences	-	-	(90)	5	(85)
At 31 December 2011	4,599	(2,314)	(2,275)	89	99

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.

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

	2011 US$'000	2010 US$'000
Deferred tax assets	4,688	4,431
Deferred tax liabilities	(4,589)	(2,123)
	99	2,308

At 31 December 2011, the Group has unused tax losses of approximately US$2,744,000 (2010: US$2,611,000) 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 2011 are tax losses of approximately US$1,349,000 (2010: US$1,327,000) 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$46,280,000 (2010: US$42,460,000).

20. INVENTORIES

	2011 US$'000	2010 US$'000
Raw materials	564	102
Work in progress	127	3
Finished goods	20,349	15,873
	21,040	15,978

21. TRADE AND OTHER RECEIVABLES

	2011 US$'000	2010 US$'000
Trade receivables	40,636	30,609
Less: Allowance for bad and doubtful debts	(331)	(215)
	40,305	30,394
Bills receivables	23,573	12,059
Purchase prepayment	2,229	2,264
Other receivables and deposits	6,903	4,597
Total trade and other receivables	73,010	49,314

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:

	2011 US$'000	2010 US$'000
0 - 90 days	37,054	26,940
91 - 365 days	3,239	3,424
Over 365 days	12	30
	40,305	30,394

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.

21. TRADE AND OTHER RECEIVABLES - continued

Included in the Group's trade receivables balance are debtors with aggregate carrying amount of US$6,400,000 (2010: US$5,457,000) 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:

	2011	2010
	US$'000	US$'000
0 - 90 days	3,340	2,406
91 - 365 days	3,053	3,025
Over 365 days	7	26
	6,400	5,457

The Group has provided full impairment for receivables that aged over 3 years from invoice date 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:

	2011	2010
	US$'000	US$'000
Balance at beginning of the reporting period	215	213
Impairment losses recognised on receivables	107	18
Amount written off as uncollectible	(5)	(16)
Currency realignment	14	-
Balance at end of the reporting period	331	215

Included in the allowance for bad and doubtful debts are individually impaired trade receivables with an aggregate balance of US$331,000 (2010: US$215,000) which have either been placed under liquidation or in severe financial difficulties. The Group does not hold any collateral over these balances.

22. AMOUNT DUE FROM A JOINTLY CONTROLLED ENTITY

As at 31 December 2010, included in amount due from a jointly controlled entity amounting to US$498,000 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, interest-free and repayable on demand.

23. HELD FOR TRADING INVESTMENTS

	2011 US$'000	2010 US$'000
Held for trading investments include:		
- Equity securities listed in the PRC	-	38

24. BANK BALANCES AND CASH/PLEDGED BANK DEPOSITS

The bank deposits and pledged bank deposits carry interest at the prevailing market rate of approximately 0.50% to 4.20% (2010: 0.36% to 2.25%) per annum.

As at 31 December 2011, included in pledged bank deposits amounting to US$nil (2010: US$1,716,000) represent deposits pledged to banks to secure short-term bank borrowings (see note 26). The remaining pledged bank deposits amounting to US$39,471,000 (2010: 2,707,000) and US$nil (2010: US$107,000) 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.

25. 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:

	2011 US$'000	2010 US$'000
0 - 90 days	10,276	232
91 - 365 days	322	3
Over 365 days	95	8
	10,693	243
Payroll and welfare payables	4,643	2,746
Other tax payables	3,192	140
Other payables and accruals	9,882	5,123
	28,410	8,252

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

26. BANK BORROWINGS - SECURED

	2011 US$'000	2010 US$'000
Advanced from banks on discounted bills receivables with recourse	39,994	2,780
Bank loans	-	1,481
Carrying amount repayable within one year	39,994	4,261

Bank borrowings comprise borrowing that are denominated in:

	2011 US$'000	2010 US$'000
US$	24,270	4,261
RMB	15,724	-
	39,994	4,261

Advanced from banks on bills receivables with carrying amount of US$39,994,000 (2010: US$2,780,000), carried fixed interest at a range from 1.98% to 3.04% (2010: 1.39% to 1.98%) per annum.

As at 31 December 2010, the remaining bank loans with carrying amount of US$1,481,000 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% per annum.

As at 31 December 2010, the bank borrowings are secured by the Group's pledged bank deposits amounting to US$1,716,000.

27. DEFERRED CONSIDERATION PAYABLES

	2011 US$'000	2010 US$'000
Non-current	4,121	4,627
Current	1,147	1,198
	5,268	5,825

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 17(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 2011, the carrying value amounting to US$5,135,000 (2010: US$5,657,000) is included in deferred consideration payables.

The remaining deferred consideration payables represented consideration for the acquisition of an associate, Ophol.

28. DERIVATIVE FINANCIAL INSTRUMENTS

Derivative under hedge accounting

	2011	2010
	US$'000	US$'000
Cash flow hedges		
- Interest rate swaps	-	24
- Foreign currency forward contracts	645	24
	645	48

(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 2011

Notional amount	Maturity	Swaps
Nil		

At 31 December 2010

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

(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 2011

Notional amount	Maturity	Exchange rates
Buy US$11,506,000	13 January 2012	US$1: RMB6.470
Buy US$12,764,000	27 February 2012	US$1: RMB6.444

At 31 December 2010

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

29. SHARE CAPITAL

	Number of shares '000	Amount US$'000
Authorised share capital:		
At 1 January 2010	1,000,000	100,000
Increase in authorised share capital (note 3)	19,000,000	-
At 31 December 2010 and 2011	20,000,000	100,000
Issued and fully paid:		
At 1 January 2010	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
Exercise of share options (note 6)	14,174	71
Issue of shares in consideration of acquisition of a subsidiary (note 7)	130,000	650
Bonus issue (note 8)	321,966	1,610
	1,609,831	8,049

Notes:

(1) On 14 May 2010, 11,835 new ordinary shares of US$0.10 of the Company were issued at 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 38).

(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 of the Company. The fair value of the ordinary shares of the Company was determined using the market price at the date of acquisition.

(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.

29. SHARE CAPITAL - continued

Notes: - continued

(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.

(6) On 7 March 2011, Mr. Chen Hong Bing ("Mr. Chen"), a director and shareholder of the Company, exercised the share options of 14,173,900 shares at an exercise price of GBP0.069 per share (equivalent to US$0.11 per share). The closing price of the Company's shares at dates on which the options were exercised was HK$6.79.

(7) On 19 April 2011, pursuant to a share purchase agreement entered into on 3 April 2011, the Company issued 130,000,000 new ordinary shares of the Company with a par value of US$0.005 each as part of the consideration for the acquisition of 100% equity interest in Great Move from an independent third party, Glitter Long Limited (see note 34(a)). The fair value of the consideration in the form of 130,000,000 ordinary shares of the Company was determined using the market price of the ordinary shares at the date of acquisition that is HK$8.58 (equivalent to US$1.103) per share.

(8) On 28 September 2011, the bonus issue has been distributed on the basis of 1 bonus share for every 4 shares held. Upon the exercise of the bonus issue, the bonus issue was credited as fully paid by way of capitalisation of an amount in the share premium account. Accordingly, 321,966,335 bonus shares were issued under the bonus issue and the new ordinary shares were calculated based on the par value of US$0.005 each.

All the shares which were issued by the Company during the year ended 31 December 2011 and 2010 rank pari passu with each other in all respects.

30. 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 five years which is vested on 26 June 2007 and 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.

On 9 March 2009, Mr. Chen Hong Bing, a director of the Company, acquired the share options of 708,695 shares from Evolution.

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 share and GBP0.069 per share respectively to reflect the share sub-division (note 29) and the share option has been fully exercised on 7 March 2011.

31. 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 Consultancy Inc. ("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 29) 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 expense 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.

32. 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.

33. FINANCIAL INSTRUMENTS

Categories of financial instruments

	2011 US$'000	2010 US$'000
Financial assets		
Loans and receivable (including cash and cash equivalents)	201,255	181,643
Held-for-trading financial assets	-	38
Financial liabilities		
Derivative instruments in designated hedge accounting relationship	(645)	(48)
Others financial liabilities measured at amortised cost	(59,790)	(10,960)

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.

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$nil (2010: US$1,481,000) carrying at floating rates (see note 26 and note 28(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 63.0% (2010: 81.7%) 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 currently has not entered into any foreign currency forward contracts to hedge against foreign currency risk. Management will consider hedging foreign currency exposure should the need arise.

The Group has entered into appropriate hedging instruments, mentioned in note 28(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 maximise hedged effectiveness (see note 28 (ii) for details).

33. 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 (that include trade and other payables and import trade loans but do not include any hedging instruments) at the reporting date are as follows:

	Currency	Assets 2011 US$'000	Assets 2010 US$'000	Liabilities 2011 US$'000	Liabilities 2010 US$'000
US dollars	US$	99	461	24,270	4,261
Euro	EURO	15	475	695	-
HK dollars	HK$	15	30,054	-	-

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% (2010: 1%) 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% (2010: 1%) change in foreign currency rates. The sensitivity analysis includes bank balances, trade and other payables and bank borrowings of which the foreign currency exposures are not hedged with hedging instruments. A positive number below indicates an increase in post-tax profit for the year where the RMB strengthens 1% (2010: 1%) against the relevant currency. If there is a 1% (2010: 1%) weakening in RMB against the relevant foreign currencies, there would be an equal and opposite impact on the result for the year:

	2011 US$'000	2010 US$'000
US dollars	242	38
Euro	7	(4)
HK dollars	-	(301)

In management's opinion, the sensitivity analysis is unrepresentative of the inherent foreign exchange risk as the year end exposure does not reflect the exposure during the year.

33. 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 2011 and 2010 would increase/decrease by US$1,214,000 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 2011 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.

33. 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.

	Repayable on demand or less than 1 year	1 to 5 years	Over 5 years	Total undiscounted cash flows	Carrying amount at 31 December 2011
	US$'000	US$'000	US$'000	US$'000	US$'000
As at 31 December 2011					
Trade and other payables	14,528	-	-	14,528	14,528
Deferred consideration payables	1,147	3,879	510	5,536	5,268
Fixed interest rate borrowings	39,994	-	-	39,994	39,994
	55,669	3,879	510	60,058	59,790
Derivatives - net settlement					
Foreign currency forward contracts	645	-	-	645	645

33. FINANCIAL INSTRUMENTS - continued

Financial risk management objectives and policies - continued

Liquidity risk - continued

	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 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

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.

33. FINANCIAL INSTRUMENTS - continued

Fair value - continued

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 2011		31 December 2010	
	Level 1	Level 2	Level 1	Level 2
	US$'000	US$'000	US$'000	US$'000
Held-for-trading investments				
Listed equity securities	-	-	38	-
Derivative financial instruments	-	645	-	48

There were no transfers between Level 1 and 2 for the year ended 31 December 2011 and 2010.

34. ACQUISITION OF SUBSIDIARIES

(a) On 3 April 2011, the Group acquired an 100% interest in Great Move from an independent third party. Great Move is an investment holding company. The principal investment of Great Move is 100% equity interest in Kangzhe Tianjin which is principally engaged in marketing, promotion and sale of prescription pharmaceutical products through network of agents/distributors and was acquired with the objective of significantly improving the Group's product portfolios and sales and promotion network.

Consideration transferred

	US$'000
Cash	62,703
Shares of the Company (note 1)	143,353
Total	206,056

Note 1: The vendor undertakes to the Group that it will not, and shall procure that those persons to whom the consideration shares are allotted and issued will not, at any time during a period of six months from the acquisition date, dispose of or encumber any of consideration shares without the prior written consent of the Company.

Assets acquired and liabilities recognised at the date of acquisition are as follows:

	US$'000
Property, plant and equipment	69
Intangible assets	28,301
Bank balances and cash	12,673
Trade and other receivables	6,634
Inventories	1,673
Trade and other payables	(5,973)
Deferred consideration payable (note 2)	(11,439)
Deferred tax liabilities	(2,160)
Tax payables	(700)
	29,078

Note 2: The amount represents the outstanding deferred consideration payable for acquisition of intangible assets. The amount has been fully settled during the year ended 31 December 2011.

The fair value of trade and other receivables at the date of acquisition is equal to the gross contractual amounts of those trade and other receivables acquired at the date of acquisition.

34. ACQUISITION OF SUBSIDIARIES - continued

Goodwill arising on acquisition

	US$'000
Consideration transferred	206,056
Less: fair value of identifiable net assets acquired	(29,078)
Goodwill arising on acquisition	176,978

Goodwill arose in the acquisition of Great Move mainly because of the promotion and sales network and the top management under the business model of Great Move that would bring along synergistic effect through the combination. In addition, the consideration paid for the combination effectively included amounts in relation to the benefit of revenue growth, future market development and the assembled workforce of Great Move.

These benefits are not recognised separately from goodwill because they do not meet the recognition criteria for identifiable intangible assets.

None of the goodwill arising on these acquisitions is expected to be deductible for tax purposes.

Net cash outflow arising on acquisition

	US$'000
Consideration paid in cash	62,703
Less: cash and cash equivalent balances acquired	(12,673)
	50,030

Impact of acquisition on the results of the Group

Included in the profit for the year is US$13,656,000 attributable to Great Move. Revenue for the year includes US$36,308,000 generated from Great Move.

Had the acquisition of Great Move been completed at 1 January 2011, total group revenue for the year would have been US$221 million, and profit for the year would have been US$65 million. The pro forma information is for illustrative purposes only and is not necessarily an indication of revenue and results of operations of the Group that actually would have been achieved had the acquisition been completed at 1 January 2011, nor is intended to be a projection of future results.

In determining the 'pro-forma' revenue and profit of the Group had Great Move been acquired at the beginning of the current year, the directors have calculated depreciation and amortisation of plant and equipment and intangible assets acquired on the basis of the fair values arising in the initial accounting for the business combination rather than the carrying amounts recognised in the pre-acquisition financial statements.

34. ACQUISITION OF SUBSIDIARIES - continued

(b) On 30 April 2011, the Group acquired an 51% interest in Kangzhe Guangming from independent third party. Kangzhe Guangming is principally engaged in production and distribution of drugs and was acquired with the objective of significantly improving the Group's product portfolios.

Consideration transferred

	US$'000
Cash	4,616

Assets acquired and liabilities recognised at the date of acquisition are as follows:

	US$'000
Property, plant and equipment	2,842
Intangible assets	2,093
Prepaid lease payments	1,290
Bank balances and cash	4,642
Trade and other receivables	570
Inventories	1,068
Tax recoverable	116
Trade and other payables	(2,090)
Bank borrowings	(4,493)
Deferred tax liabilities	(273)
	5,765

In the opinion of the directors of the Company, the fair value of the receivables acquired (which principally comprised of trade and other receivables) approximates to the gross contractual amounts, the best estimate at acquisition date of the contractual cash flows of the receivables are expected to be collected.

	US$'000
Consideration transferred	4,616
Plus: non-controlling interests	2,426
Less: fair value of identifiable net assets acquired	(5,765)
Goodwill arising on acquisition	1,277

The non-controlling interest (49%) in Kangzhe Guangming recognised at the acquisition date was measured by reference to the share of the fair value of the identifiable assets acquired and the liabilities assumed which amounted to US$2,426,000.

34. ACQUISITION OF SUBSIDIARIES - continued

Net cash inflow arising on acquisition

	US$'000
Consideration paid in cash	4,616
Less: cash and cash equivalent balances acquired	(4,642)
	(26)

The goodwill is attributable to the anticipated profitability arising from the distribution of the products of Kangzhe Guangming in the new markets and the future operating synergies from the combination. These benefits are not recognised separately from goodwill as they do not meet the recognition criteria for identifiable intangible assets.

Impact of acquisition on the results of the Group

Included in the profit for the year is US$137,000 attributable to Kangzhe Guangming. Revenue for the period includes US$3,690,000 generated from Kangzhe Guangming.

Had the acquisition of Kangzhe Guangming been completed at 1 January 2011, the total group revenue for the year would have been US$212 million, and profit for the year would have been US$62 million. The proforma information is for illustrative purposes only and is not necessarily an indication of revenue and results of operations of the Group that actually would have been achieved had the acquisition been completed at 1 January 2011, nor is intended to be a projection of future results.

In determining the 'pro-forma' revenue and profit of the Group had Kangzhe Guangming been acquired at the beginning of the current reporting period, the directors have calculated depreciation and amortisation of plant and equipment and intangible assets acquired on the basis of the fair values arising in the initial accounting for the business combination rather than the carrying amounts recognised in the pre-acquisition financial statements.

35. 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:

	2011 US$'000	2010 US$'000
Within one year	574	508
In the second to fifth years inclusive	326	275
	900	783

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

36. RELATED PARTY TRANSACTIONS

(a) Apart from details of the balances with related parties disclosed in note 22, the Group entered into the following transactions with related parties during the year:

Name of related company	Relationship	Nature of transactions	2011 US$'000	2010 US$'000
Ophol	Associate	Finance cost	261	290
Guangdong Lantai	Jointly controlled entity	Sales of goods	385	1,238
Hui Ki Fat	Director and shareholder	Consideration paid for acquisition of additional interest in a subsidiary	-	2,325

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

37. 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$1,003,000 (2010: US$790,000).

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.

(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 2011, the Company contributed cash amounting to US$153,000 (2010: US$104,000) to the Fund and which were recognised as key employee benefit expenses in the profit or loss in the consolidated statement of comprehensive income. On the other hand, the Scheme subscribed nil shares and 11,835 shares of the Company during the year ended 31 December 2011 and 2010 respectively (see note 29).

39. SUBSIDIARIES OF THE COMPANY

As at 31 December 2011 and 31 December 2010, 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 2011	31 December 2010	31 December 2011		31 December 2010		
				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	RMB350,000,000	-	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%	-	100%	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
Great move (note 3)	British Virgin Islands	US$10,000	-	-	100%	-	-	Investment holding
Generous Wealth Limited (note 3)	Hong Kong	HK$1	-	-	100%	-	-	Investment holding
Kangzhe Tianjin (note 3)	PRC	RMB100,000,000	-	-	100%	-	-	Trading of drugs
Kangzhe Guangming (note 4)	PRC	RMB18,370,000	-	-	51%	-	-	Production of medicines

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.
3. The subsidiaries are acquired on 3 April 2011 (Note 34(a)).
4. The subsidiary is acquired on 30 April 2011 (Note 34(b)).

40. EVENTS AFTER THE REPORTING PERIOD

Subsequent to the end of the reporting period, the directors recommended a bonus issue of shares on the basis of one bonus share for every two existing share in issue on 4 May 2012. The bonus issue is conditional upon (a) the passing of an ordinary resolution by shareholders at an annual general meeting that is scheduled to be held on 25 April 2012, and (b) the Listing Committee of the Stock Exchange of Hong Kong Limited granting the listing of, and permission to deal in, the bonus shares. The bonus shares will be credited as fully paid by way of capitalisation of an amount equal to the total par value of the bonus shares in the share premium account of the Company. The bonus shares, upon issued, will rank pari passu in all respects with the then existing shares in issue as at the record date, except that they will not rank for the proposed cash dividend of the Company for the year ended 31 December 2011.