BUSINESS REVIEW

1. **Production & Sales Operation**

The Group continued to optimize its production process and production management for the production of cephalosporin medicines in powder for injection form so as to explore underutilized capacities for satisfying demand in the market to the greatest extent. Total output for cephalosporin medicines in powder for injection form amounted to 63,101,300 vials in year 2003, representing an increase of 85% over 33,941,600 vials in the previous year. Sales of cephalosporins in powder for injection forms was RMB230,976,000, representing an increase of 20% as compared with last year.

The new bulk medicine workshop commenced operation in early 2003. The Group fully leveraged on the additional capacity and expanded its production of bulk medicine on an extensive scale. A total of 223.10 tonnes of bulk medicine was produced in year 2003, which grew by 2.63 times over 61.49 tonnes in the previous year. Not only has the Group consolidated its leading position in the market of cefoperazone sodium, but also rapidly established its market share for ceftriaxone sodium by capitalizing on the advantages of its brand. Its market share has grown to over 25%. Sales of bulk medicines recorded by the Group during the year 2003 was RMB209,950,000, representing a growth of 86% compared with last year.

Output of preparation medicines in oral form (system specific medicines) was 100,684,900 tablets/ capsules for the year, which was increased by 1.06 times over 48,758,500 tablets/ capsules in the previous year. Sales of preparation medicines in oral form (system specific medicines) was RMB48,681,000 in year 2003, an increase of 122% as compared with last year.

2. **Products In The Pipeline**

During 2003, the Group obtained 7 clinical permits, 24 production and supplementary production permits from the State Food and Drug Administration of the PRC (“SFDA”). Of which, the Company succeeded in the R&D and launched three anti-infective drugs, namely sparfloxacin lactate, ceftazidime, and sulbactam sodium as well as compound ranitidine capsules, a medicine for the treatment of gastric ulcers. Currently, the Group has 47 species of medicines, 10 of which are new medicines. In addition to compound ranitidine capsules, more than 10 R&D projects, including a project for the fourth generation cephalosporins, are currently in the pipeline as planned. Another important task for the R&D team is to continue with the optimization of the production process, so as to enhance the quality and reduce the cost accordingly. The production process of intermediate for several anti-infective drugs and bulk medicines are further optimize, and thus their advantages in terms of quality and cost were consolidated.

3. **Expansion of Production Facilities**

The construction of the new bulk medicine workshop, which successfully passed the national GMP certification, has six production lines and an annual production capacity of 235 tonnes, was completed and commenced production in the first quarter of 2003. The construction of the new workshop for the production of cephalosporin medicines in powder for injection forms, which successfully passed the GMP certification of SFDA, has 12 production lines and an annual production capacity of 235,000,000 vials, was completed in the fourth quarter of 2003. Trial operation was successfully completed for one time in the fourth quarter of 2003. Equipment installation for the synthetic workshop with one production line for specific medicine and annual production capacity of 20 tonnes was also completed. Equipment testing and system commissioning is currently undergoing.

PROSPECTS

The Group's principal product, cephalosporins, has been the most popular medicine within its category in the PRC. It is anticipated that the demand of cephalosporins will enjoy greater growth. Various cephalosporin products of the Group have adopted our core technology, which has been enjoying obvious competitive advantages. Potential in the growth of sales remained high. Following the operation of a new workshop for the production of powder for injection commenced, sales of medicine in powder for injection form will not be subjected to limit in production capacity. However, following competitions in the cephalosporin medicines becoming more intensive, production will be focused on the integrated and consolidated pharmaceutical groups with the business model of "intermediate-bulk medicine-preparation medicine". The Group will continue to devote in strengthening antibiotics as a solid profit foundation.

Apart from antibiotics, system specific medicine is another foundation to support the Group's profitability. Currently, the sales of system specific medicines represents nearly 10% of the total turnover. The Group is currently consolidating its sales resources and strengthening capabilities in the development of market for system specific medicines. Amlodipine besylate, which was launched in late 2002, as well as compound ranitidine capsules, a medicine for the treatment of gastric ulcers launched in late 2003, are both international classic medicines. It is believed that with the expansion in the extent of marketing and promotion activities, the Group will achieve remarkable results. Following the increase in the sales of system specific medicines with high profit margin, the Group expects the overall gross profit margin will be lifted.

FINANCIAL REVIEW

Sales and Gross Profit

During the year ended 31 December 2003 ("the Reported Year"), the Group recorded sales income of approximately RMB491,388,000, representing an increase of 50% as compared with the previous year. Gross profit was approximately RMB205,903,000, an increase of 19% as compared with the previous year. Gross profit margin was 42% (2002: 53%). The main reasons for the fall in gross profit margin are as follows: firstly, the Group took the initiative in reducing prices to consolidate and increase market share; secondly, the Group increased proportion of sales of bulk medicine that have relatively lower gross profit margin; and thirdly, reductions in unit cost was less than reductions in sales prices of our products. The Group will continue to optimize production technology, strengthen production process management, and reduce material costs, with the effect that there have been obvious reductions in the unit costs of the products.

During the Reported Year, sales of bulk medicine amounted to RMB209,950,000, representing an increase of 86% as compared with RMB113,176,000 of year 2002. Sales of bulk medicine accounted for 43% of total sales (2002: 35%). Gross margin of bulk medicine in the Reported Year was approximately 20% (2002: 37%).

During the Reported Year, sales of preparation medicine powder for injection form amounted to RMB230,976,000, representing an increase of 20% as compared with year 2002. Sales of powder for injection form accounted for 47% of total sales (2002: 59%). Gross margin of preparation medicine powder for injection form in the Reported Year was approximately 55% (2002: 60%).

During the Reported Year, sales of system specific medicine amounted to RMB48,681,000, representing a 1.22 times increase as compared with RMB21,888,000 of year 2002. Sales of system specific medicine accounted for 10% of total sales (2002: 7%). Gross margin of system specific medicine in the Reported Year was approximately 78% (2002: 69%).

The two anti-infective drugs launched during the Reported Year, namely ceftazidime (bulk medicine form and powder for injection form) and sparfloxacin lactate contributed turnover of RMB3,428,000 and RMB3,985,000, respectively.

Expenses

Total expenses incurred during the Reported Year amounted to approximately RMB94,346,000, an increase of 31% over the previous year. Total expenses as a percentage of sales reduced to 19% (2002: 22%).

Of which, selling and distribution costs amounted to RMB56,795,000, an increase of 9% over the previous year. Selling and distribution cost as a percentage of sales reduced to 12% (2002: 16%).

Administrative costs and other operating costs amounted to RMB36,606,000, an increase of 89% over the previous year. The increase was due to expenses incurred by Suzhou Dawnrays Chemical Co., Ltd (construction work of which commenced in the second half year of 2002), expenses incurred by the Hong Kong head office (which was set up in the second half year of 2002), and increased research and development expenditures. Financial cost amounted to RMB945,000, an increase of 81% as compared with the previous year.

Profit Attributable to Shareholders and Income Tax

During the Reported Year, profit attributable to shareholders amounted to RMB108,022,000, a growth of approximately 8% over that of the previous year. Net profit margin was 22% (2002: 31%). The reduction in net profit margin was, mainly due to the fall in gross profit margin and the fact that Suzhou Dawnrays Pharmaceuticals Co., Ltd commenced to pay income tax during the Reported Year.

In 2003, Suzhou Dawnrays Pharmaceuticals Co., Ltd started, till the end of 2005, to be subject to its 50% tax exemption at a corporate income tax rate of 12%. This is in contrast with full exemption in the previous year. Shanghai Dawnrays Chemical Co. Ltd is exempted from corporate income tax and local corporate income tax for the second year.

Analysis on return of assets

During the Reported Year, with average total assets of RMB415,166,000, the Group realised net profit attributable to shareholders of RMB108,022,000, the Return on Total Assets (defined as Net Profit Attributable to Shareholders over Average Total Assets) was 26%, and far exceeded the average level of 4.29% for the nine months ended 30 September 2003 for the chemical pharmaceutical industry in accordance with the statistics compiled by the 中國化學制藥工業協會 .

In fact, the Group capitalized on two important factors that were attributable to such Return on Total Assets: (1) Net Profit margin in the Report Year was approximately 22%; (2) rate of Total Assets Turnover (defined as Turnover over Average Total Assets) during the Reported Year was approximately 1.2 times. Turnover of funds was fast as a result of a high utilization rate in assets.

During the Report Year, Return on Equity (defined as Net Profit Attributable to Shareholders over Average Equity) was 38%.

Cashflow

The cashflows of the Group have been healthy. This was mainly attributable to the effective system of the Group established for sales management purpose, where performance appraisal of sales staff emphasized cash collection of sales money, thus reducing the aging period to a significant extent, and placing the responsibility of collection on the front-line sales staff. The Group adopted sound financial strategy, the supply of materials has credit period of three to six months. In R&D projects and market explorations, application of funds also pursued for principles of efficiency. With respect to capital expenditures on constructions of production facilities, tenders for major construction projects will be invited from the public, so as to strictly control estimation, budget and finalisation of accounts.

1) Net cash inflow from operating activities were RMB88,944,000 during the Reported Year.

2) Expenditures on construction projects and purchases of fixed assets and purchases of land-use-rights amounted to RMB64,992,000.

3) Profit distributions (including dividend paid to minority shareholders) amounted to RMB82,360,000.

4) Net proceeds from the New Issue of shares amounted to RMB155,286,000.

On 31 December 2003, the Group has monetary funds of RMB134,521,000 in hand, and no bank loans.

Liquidity, financial resources and capital structure

As at 31 December 2003, the Group's current assets amounted to approximately RMB360,141,000, whilst current liabilities was approximately RMB183,601,000. Net current assets were approximately RMB176,540,000.

As at 31 December 2003, the Group has aggregate bank facilities of approximately RMB325,000,000.

As at 31 December 2003, approximately RMB3,500,000 of the bank facility was secured over certain of the Group's properties. The pledge was subsequently released by banks in January 2004.

The debt ratio (defined as interest bearing loans and borrowings over total assets) of the Group as at 31 December 2003 was 0%.

Interest capitalized by the Group in relation to construction projects during the Reported Year was approximately RMB88,000.

As at 31 December 2003, the Group's capital commitments amounted to approximately RMB103,946,000 which will be funded by proceeds from listing and by internal resources.

Financial management, financial instruments and exchange rate risk

The Group implements a steady and prudent financial strategy. Exposure incurred during its course of financial management are managed in accordance with policies approved by the Board of Directors.

Substantially all of the revenue generating operations of the Group are normally transacted in Renminbi, which is not freely convertible into foreign currencies.

The Group's monetary assets and liabilities are normally denominated in Hong Kong Dollars, Renminbi and US Dollars.

The carrying amount of the Group's cash and cash equivalents, trade receivables and payables, other receivables and payables, borrowings and balances with related parties approximate their values because of the short maturity of these instruments.

The Group did not enter into any foreign exchange forward contracts or other hedging instruments to hedge against fluctuations, and the Group did not use any financial instruments.

Significant investments

Other than the expansion of the production facilities of Suzhou Dawnrays Pharmaceuticals Co., Ltd and establishment of a production plant for Suzhou Dawnrays Chemical Co., Ltd, as disclosed in the Company's prospectus dated 30 June 2003 under the section headed "Future Plans and Use of Proceeds", the Group did not have significant investments or material acquisitions or disposals of subsidiaries and affiliated companies during the year ended 31 December 2003.

Staff

Human resources is the most valuable assets of the Group. A professional, pragmatic, and highly efficient management team together with the staff as a whole is the Company's most valuable competitive advantage. The Group provides a competitive remuneration policy.

As at 31 December 2003, the Group employed approximately 749 employees (31 December 2002: approximately 535 employees) at market remuneration with employee benefits such as defined contribution retirement schemes, share option scheme and medical coverage. The Group provides certain of its employees in PRC with dormitory accommodation in PRC and makes monthly contribution to State unemployment insurance funds and to the State housing fund for employees in the PRC.

Total staff costs for the year were approximately RMB27,537,000 (2002: RMB15,978,000).

The Company has adopted a share option scheme. Under the share option scheme, the Eligible Persons (including the executive, non-executive and independent non-executive directors and employees of the Group (whether full time or part time)) may be granted options which enable them to subscribe for shares in the Company, up to a maximum of 10% of the shares in issue of the Company.

Options in respect of a total number of 40,000,000 shares has been granted during the year by the Company to Eligible Persons on 11 November 2003.

Charge on assets

As at 31 Decmber 2003, buildings with net book values of approximately RMB3,500,000 were pledged to banks to obtain credit facilities. The pledge was subsequently released by banks in January 2004.

As at 31 December 2002, buildings and machinery and equipment with net book values of approximately RMB17,069,000 and RMB11,764,000 respectively, were pledged to banks to obtain credit facilities.

Plans for significant investments and expected source of funding

Details of the Group's future plans for significant investments and their expected source of funding have been stated in the Company's prospectus dated 30 June 2003 under the section headed "Future Plans and Use of Proceeds".

The Group plans to construct a new workshop for the production of cephalosporins bulk medicines to further increase the Group's production capacity of cephalosporins bulk medicines from the existing 300 tonnes per annum to approximately 600 tonnes per annum. The Group plans to fund this investment by internal resources.

Other than those disclosed above, the Group did not have any plan for material investments or capital assets.

Segment information

The Group's turnover and profit for the two years ended 31 December 2003 were mainly derived from the sale of medicines by the PRC subsidiaries to customers in the PRC. The principal assets employed by the Group are located in the PRC. Accordingly, no segmental analysis by business and geographical segments is provided.

Contingent liabilities

As at 31 December 2003, the Group had no material contingent liabilities (31 December 2002: Nil).

MAJOR SUPPLIERS AND CUSTOMERS

The percentage of purchases and sales for the year ended 31 December 2003 attributable to the Group's major suppliers and customers are as follows:

Purchases	
— the largest supplier	23%
— five largest suppliers combined	47%
Sales	
— the largest customer	8%
— five largest customers combined	23%

None of the directors, their associates or any shareholder (which to the knowledge of the directors owns more than 5% of the Company's share capital) had an interest in the major suppliers or customers stated above.

USE OF PROCEEDS FROM CAPITAL RAISING

The Group raised approximately HK$146 million, net of related expenses, from the new issue and placing of 200,000,000 new shares of the Company at HK$0.8 per share in July 2003. The Company's shares were successfully listed on the Stock Exchange of Hong Kong Limited on 11 July 2003. The Directors have applied the net proceeds as to approximately HK$32 million for the expansion of production facilities of Suzhou Dawnrays Pharmaceuticals Co., Ltd and the establishment of a production plant for Suzhou Dawnrays Chemical Co., Ltd; approximately HK$5 million on research and development; and approximately HK$4 million as selling and marketing network cost. The remaining net proceeds from the new issue and the placing are currently placed with licensed banks in Hong Kong and PRC, and would be used in accordance with the intended use of proceeds as stated in the prospectus.