

Management Discussion and Analysis

The Company obtained a listing on the GEM of the Stock Exchange on 29 September, 2000, and on the Main Board of the Stock Exchange on 8 December, 2003. Over the past three years, the Group has been developing rapidly, with turnover increasing from approximately HK\$392.73 million in 2000 to approximately HK\$821.70 million in 2003, representing an increase of approximately 109.2%. Profit attributable to shareholders surged 81.3% from approximately HK\$45.13 million in 2000 to approximately HK\$81.62 million in 2003. Basic earnings per share increased from approximately HK17.6 cents in 2000 to approximately HK24.6 cents in 2003, representing an increase of approximately 39.8%. In addition to the constant sales increase from its principal products, a total of 19 new products have been successfully launched in the market since 2000. These products, contributed significantly to sales in 2003, amounting to HK\$325.50 million and accounted for 39.6% of total turnover in 2003. Among these, Mioclear eyedrops for treating eye fatigue and Tianqingfuxin for treating hepatitis, successfully launched in May, 2000 and December, 2001 respectively, have become the Group's principal products with turnover of over HK\$100 million each in 2003, while the Spring injections for the treatment of cardio-cerebral diseases and Naphazoline eyedrops (red Mioclear) for treating eye fatigue, launched in January, 2001 and January, 2003 respectively, showed strong growth potential. It is anticipated that they will become another principal products with individual turnover in excess of HK\$100 million in the near future.

The Group has five products with sales over HK\$100 million. They are namely Moisten eyedrops, Mioclear eyedrops, Diammonium Glycyrrhizinate injections and capsules, Tianqingfuxin injections and capsules, and Alprostadil injections.

CTF, JCTT, CTQ and Beijing Tide were the principal sources of earnings for the Group.

CTF

CTF is a pharmaceutical company which uses biological product—hyaluronic acid (HA) as its principal raw material and supplementary material, and holds several patents for HA-containing formulae and production methods.

For the year ended 31 December, 2003, CTF experienced steady growth in turnover by 15.1% as compared with corresponding period last year, which rose to approximately HK\$378.47 million and accounted for approximately 46.1% of the Group's turnover. Sales of principal products are expected to be promising due to an experienced and established sales team for non-prescription drugs and prescription drugs, advertising and promotion of the products and the enhancement of the corporate image. Sales of Moisten eyedrops for anti-bacteria and anti-inflammation remained stable with a sales of HK\$116 million. Sales of Mioclear eyedrops for the relief of eye fatigue continued to grow, reaching HK\$100 million. A new product, red Mioclear eyedrops also for the relief of eye fatigue, was launched in the market in 2003, and achieved annual sales of over HK\$45 million. Sales from the newly launched Helen eyedrops (Levofloxacin Hydrochloride Eye Drops) for anti-bacteria and anti-inflammation problems reached over HK\$10 million. The Group currently manufactures 18

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products for eye treatments, which contribute over 80% of total sales of CTF. During the review period, the osteoarthritis medicine Sofast (Sodium Hyaluronate) Injection also flourished, with sales of over HK\$50 million, an increase of over 27% against the corresponding period last year. The new product Jiarui (Butenafine Hydrochloride Ointment) for anti-epiphyte, a medicine for external use to treat skin diseases, has been granted new medicine production approval from the State Food and Drug Administration of the PRC ("SFDA"), and is scheduled for launch in April, 2004. It is forecast to be yet another principal product for CTF along with its other products for the treatment of eye diseases.

CTF's raw material synthesis workshops, HA refining workshops, heparin sodium refining workshops, bottle production, filling and sealing three-in-one eyedrops workshops are under construction in Jinan High and New Technology Development Zone (濟南高新技術開發區). Their respective GMP Certificates are expected to be obtained in the first half of 2004.

JCTT

JCTT is a pharmaceutical company that focuses mainly on the modernised Chinese medicine, chemical medicine and modern health-care products.

For the year ended 31 December, 2003, JCTT continuously achieved a satisfactory performance with turnover increasing 19.4% to approximately HK\$434.96 million, accounting for 52.9% of the Group's total turnover. In 2003, JCTT reorganized its sales structure, and divided its sales teams by product into different departments. All the departments shared market resources and operated with total professionalism. The hepatitis medicines department, which accounted for over 80% of the sales income of the division, has been able to focus more strongly on the market development of hepatitis medicines. With increased human resources and marketing effort, JCTT also increased the number of its sales representative offices by 38. Though overall sales performance was affected by SARS outbreak, adversely affecting the sales of prescription medicines such as medicines for treating hepatitis, sales from hepatitis medicines still experienced significant growth during the period under review. Sales of its principal products, Diammonium Glycyrrhizinate injections and capsules, also recorded a stable increase. Tianqingfuxin, launched in December, 2001, sales was increased by 106.3% as compared with last year and amounted to HK\$131 million (representing approximately 16.0% of the total turnover of the Group) becoming another principal product of the Group. The new drugs department also put 16 sales representative offices into place, which led to encouraging sales. Sales of Spring injections amounted to HK\$28 million, representing an increase of 72% over the corresponding period last year.

JCTT increased workshop capacity for powder and granule medicines in 2003, and obtained GMP certification from SFDA for its material synthesis medicines, power medicines and granule medicines in July, 2003.

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In September, 2003, JCTT received the "Torch Programme Best High and New Tech Enterprise" award upon the 15th anniversary of the Torch Programme, by the PRC's Ministry of Science and Technology.

Nanjing Chia Tai Tianqing Pharmaceutical Co., Ltd. ("NJCTT")

The production workshops for PVC-free soft bags for intravenous injections were certified on 9 October, 2003, receiving their GMP certificates from the SFDA. Production officially commenced after a year of trial production, with adjustments in the product structure and training of the sales team. In December, 2003, NJCTT also obtained approval for production of Puerarin glucose (Spring) PVC-free soft bags for intravenous injections. In view of these developments, NJCTT expects to enjoy promising performances and market expansion this year.

Beijing Tide

Beijing Tide, restructured in October, 2003, is principally engaged in the production and sales of Alprostadil (凱時) injection, a kind of target and sustained release preparation of Prostaglandin E1 ("PGE1") (脂微球靶向緩釋製劑) that active substance of Lipo-microspheres PGE1 can be used for angiocardopathy. This product has adopted an internationally-advanced target preparation of PGE1 invented by, and patent technology of which was transferred from, Professor Mizushima Yataka, a renowned medical scientist in Japan. Capitalizing on this start-of-the-art technology and its exclusiveness, the product shows improved treatment results when compared to other similar products. With an effective marketing strategy, Alprostadil recorded significant growth in sales and profit. Turnover for 2003 rose to approximately HK\$183.32 million, representing an increase of approximately 39.4% over the corresponding period last year.

The new factory, located in Beijing Economy Development Zone (北京經濟開發區), is under construction, and it is expected to be completed by the end of 2004. It will be capable of producing 10 million injections, 500 million tablets and capsules, per annum.

R&D

The year 2003 saw the greatest successes for the Group in R&D. Numerous R&D projects came to a positive conclusion leading to successful completed results. The Group also has the largest numbers of cases under research, in its history. It also obtained numerous patents and received substantial governmental scientific research funding.

There were 12 approvals for production of new drugs and 22 approvals for clinical research from the SFDA, one health-care food certificate from the Ministry of Public Health of the PRC, 30 research cases are, and soon will be under, clinical trials, 32 invention patent application acceptance notifications have been received from the State Intellectual Property Office together with 3 new

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practical patent acceptance notifications. Among these achievements are 18 invention patent application acceptance notifications, involving 22 new products awarded to Beijing Chia Tai Green Continent Pharmaceutical Co., Ltd. ("CT Green Continent") by the State Intellectual Property Office. In March, 2003, CT Green Continent was certified as a high and new technology enterprise by Beijing Science and Technology Committee.

JCTT was granted a clinical research fund for drugs innovation and modernization of a significant range of traditional Chinese medicines, with RMB1.2 million being received under the National High-Tech Research and Development Plan of the PRC (the National Plan-863). The funds are intended for use in the clinical research of hepatitis medication, under the Tenth Five-Year Plan.

JCTT's postdoctoral R&D center is currently staffed by 3 researchers who hold doctor's degrees.

The pharmaceutical research project for the treatment of hepatitis using biotechnology in genetic engineering was jointly developed by China Biotech & Drug Development Limited in conjunction with Hong Kong Polytechnic University. The project has been granted a subsidy of HK\$1.56 million by the Innovation and Technology Commission of Hong Kong Special Administrative Region.

CAPTIAL STRUCTURE

On 8 January, 2003, a total of 12,000,000 share options of HK\$0.10 each had been exercised at HK\$0.74 per share. The proceeds before expenses amounted to HK\$8,880,000 and the share capital and share premium were increased by HK\$1,200,000 and HK\$7,680,000 respectively.

The Group repaid all the bank loans during the year (2002: approximately HK\$4.71 million).

LIQUIDITY AND FINANCIAL RESOURCES

The Group's liquidity remains strong. During the year, the Group's primary source of funds was cash derived from operating activities and funds raised by the issuance of convertible bonds in 2003. As at 31 December, 2003, the Group's bank balance and cash in hand was approximately HK\$288.85 million (2002: approximately HK\$280.53 million).

CAPITAL COMMITMENT

The Group's capital expenditure commitments amounted to approximately HK\$64.18 million as at 31 December, 2003 (2002: approximately HK\$21.38 million). The Group has adequate financial resources to fund its capital expenditure commitment from existing cash resources and cash flows generated from its operations.

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CHARGE ON ASSETS

The Group did not have any charges on assets as at 31 December, 2003 (2002: nil).

CONTINGENT LIABILITIES

At the balance sheet date, neither the Group, nor the Company had any significant contingent liabilities (2002: nil).

ASSETS AND GEARING RATIO

As at 31 December, 2003, total assets of the Group amounted to approximately HK\$736.00 million (2002: approximately HK\$593.99 million) whereas total liabilities amounted to approximately HK\$239.67 million (2002: approximately HK\$171.45 million). The gearing ratio (total liabilities over total assets) was approximately 32.6% (2002: approximately 28.9%).

EMPLOYEE AND REMUNERATION POLICIES

As at 31 December, 2003, the Group had about 2,629 employees (2002: 2,227). The Group remunerates its employees based on their performance, experience and the prevailing market rates. Other employee benefits include mandatory provident fund, insurance and medical coverage, subsidized training programmes as well as a share option scheme.

Total staff costs (including Directors' remuneration) for the year were HK\$105,541,000 (2002: HK\$97,062,000).

EXPOSURE TO FLUCTUATIONS IN EXCHANGE RATES

Most of the assets and liabilities of the Group were denominated in Renminbi and HK dollars. In the PRC, foreign investment enterprises are authorized to convert Renminbi to foreign currency in respect of current account items (including payment of dividend and profit to the foreign joint venture partner). The Directors consider that the Group is not significantly exposed to foreign currency risk and no hedging or other alternatives have been implemented.