MANAGEMENT DISCUSSION AND ANALYSIS

Engaged principally in the research and development, manufacture and sales of gynecological medicine and medicinal healthcare products for women in the People's Republic of China ("**PRC**"), the Group has been continuously capitalising in its national sales and marketing network in the year ended 30 June 2004 ("**Year**").

MARKET REVIEW

During the financial year, major developments in the PRC pharmaceutical industry include the following:

1. According to the PRC regulations, pharmaceutical factories that could not obtain Good Manufacturing Practice ("**GMP**") certification by the end of June 2004 were obliged to cease operations, resulting in the reduction of the number of pharmaceutical manufacturers from over 6,000 to about 2,000, creating more market opportunities for pharmaceutical manufacturers that complied with the GMP Standards such as the Group;

2. Because of strict protective regulations introduced by the PRC Government against infringement of intellectual property rights of western medicines, western medicine manufacturers in the PRC are under severe pressure and fierce competition. Thus, manufacturers having proprietary rights of the pharmaceutical products they produce and manufacturers of Chinese Medicines have better growth potentials;

3. Mergers and acquisitions have become the dominant trend in the pharmaceutical industry; it is observed that acquisitions occurred not only among manufacturers, but also among manufacturers and distributors, causing more concentration and integration; and

4. Owing to the change in medicine classification (between prescription medicines and over-the-counter ("**OTC**") medicines), pharmaceutical manufacturers and distributors with large range of products have become more competitive.

BUSINESS REVIEW

During the Year, the Group recorded satisfactory results despite the challenge of severe market competition. Our encouraging performance is attributable to, we believe, the Group's range of competitive products and its three-pronged business-growth strategy, comprising (1) **Prestigious Brand Name Building**: apart from our strong hospital heritage, OTC operations started to expand our brand and increase consumer awareness; (2) **Legend Products**: we have achieved a leading position in gynecological therapeutic areas especially in anti-viral and feminine oncology treatment. Three new products were launched during the year under review and a strong prescription drug is in the pipeline; and (3) **Nationwide Sales Network**: sales and distribution network expanded through both acquisitions and organic growth.

The successful acquisition of two sales and distribution enterprises of pharmaceutical products during the Year, together with another acquisition well underway, are strategic accomplishments that have afforded immediate access to established sales and distribution networks, and the expansion of its scales of sales and production in gynecological drugs as well as its profitability. Additionally, these acquisitions have facilitated reduction in operating costs and more efficient utilisation of operating resources by way of vertical integration, thus enhancing the competitiveness of the Group as a whole and thus its profit margin.

MANAGEMENT DISCUSSION AND ANALYSIS

FINANCIAL PERFORMANCE

The Group has achieved continuing growth in annual turnover and net profit for the three-year period from 2001 to 2004, at an annual compound growth rate of 19.3% and 8.5% in turnover and net profit of the Group's products respectively. For the year under review, the Group recorded a total turnover of approximately HK$507.0 million, approximately HK$273.2 million (2003: approximately HK$219.0 million) of which was attributable to the turnover of the Group's products, representing a growth of 24.7% over last year, and approximately HK$233.8 million of which was revenue from the trading activities.

Gross profit of the Group's products for the Year was approximately HK$147.0 million, representing a growth of 4.2% over that for last year of approximately HK$141.0 million. The gross profit of trading products for the Year was approximately HK$15.3 million. Profit attributable to shareholders of the Group for the Year was approximately HK$95.0 million (2003: approximately HK$85.9 million), representing an increase of 10.6% from that of last year.

PRESCRIPTION DRUGS

Gynecological Anti-inflammatory Products

The **Yeosure Series（日舒安系列）** product line, which offers a comprehensive range of products with different therapeutic functions targeted at women of all ages, retained its major contributory position to the Group's proprietary products turnover. Amongst the popular Yeosure products are **Yeosure Natural Medicine Lotion（日舒安洗液）** and **Yeosure Moistened Toilet Towel（日舒安濕巾）**, gynecological anti-inflammatory products. The **Yeosure Series** gynecological anti-inflammatory product line recorded sales of approximately HK$102.3 million, representing 37.4% of total turnover of the Group's products and an increase of 13.0% from that of last year.

Gynecological Endocrine Products

Yeosure Puerperant's Health Drink（日舒安婦康沖劑）, a gynecological endocrine product, produced total sales of approximately HK$15.7 million, representing 5.8% of the total turnover of the Group's products.

Gynecological Anti-tumour Products

Jin Xi Su（金喜素） and **Qiang Xi（強喜）**, **Camptothecine Series（喜樹鹼系列）**, naturally sourced gynecological anti-tumour injection medicines, brought in total sales of approximately HK$75.4 million, representing about 27.6% of the Group's total products turnover and an increase of 17.4% compared to last year. Gross profit margin of the Camptothecine Series of products for the year was 66.5%.

MANAGEMENT DISCUSSION AND ANALYSIS

Medicine for Children

Cefadroxil Granules（穀達顆粒）, an antibiotic for children, produced total sales of approximately HK$28.4 million, representing 10.4% of the total turnover of the Group's products and an increase of 18.6% from that of last year.

Other Drugs

A new product for gynecological disease and a Chinese medicine introduced during the Year, **Youdi Lotion（疣迪搽劑）**, for detoxifying, resolving blood stasis and activating blood circulation and **Biejia Xiaozhi Capsules（鱉甲消痔膠囊）**, for eliminating heat, detoxifying detumescence and relieving pain, attributed sales of approximately HK$17.1 million, representing 6.3% of the total turnover of the Group's products.

In April 2004, Guizhou Hanfang Medicine Manufacture Co., Ltd.（貴州漢方製藥有限公司）("**GHMM**"), a wholly owned subsidiary of the Company, was appointed the exclusive manufacturer of **Methadone（美沙酮）** for the Guizhou Test Treatment Centre for Drug Abuse Patients by the State Food and Drug Administration of the PRC（中國國家食品藥品監督管理局）("**SFDA**"). The production of Methadone for the Guizhou Test Treatment Centre for Drug Abuse Patients commenced in June 2004. It is expected that profit will be generated from such manufacturing activity when more participants join the program.

OVER-THE-COUNTER DRUGS

Gynecological Endocrine Products

Sales of **Huangqi Granules（黃芪顆粒）**, a gynecological endocrine product, was approximately HK$28.4 million, representing 10.4% of total sales of the Group's products and an increase by 92.6% compared to that of last year. Regarding sales of the product in the Hong Kong market, it is expected that the agreement with the Hong Kong agent will be finalised in the present financial year as all basic terms and conditions have been agreed.

MERGERS AND ACQUISITIONS

The Group has successfully acquired Hubei Kanglai Medicine Company Limited（湖北康萊醫藥有限公司）("**Kanglai Medicine**") through the acquisition of 51.0% equity interest in Shenzhen Xinchuang Bio-Pharmaceutical Pioneering Investment Company Limited（深圳市新創生物醫藥創業投資有限公司）, which holds approximately 51.7% equity interest in Kanglai Medicine. The Group has reached agreement for the acquisition of 70.0% equity interest in Guangdong Qunhe Pharmaceutical Company Limited（廣東群禾藥業有限公司）("**Guangdong Qunhe**"). The acquisitions of Kanglai Medicine and Guangdong Qunhe give us immediate access to their well established sales and distribution networks, thereby expanding the Group's existing network considerably and allowing the Group to improve its operating efficiency and expand our own product sales into the areas they cover.

MANAGEMENT DISCUSSION AND ANALYSIS

RESEARCH AND DEVELOPMENT

The Group emphasises on the importance of new product development. Through the strengthening of its research and development capabilities in the manner referred to below, the Group is able to further expand its product mix and sources of revenue. The Group has collaborated with leading research institutes like the Institute of Materia Medica of the Chinese Academy of Medical Sciences (中國醫學科學院藥物研究所), and during the Year, the Group successfully obtained the approved pharmaceutical numbers (國家藥品批准文號) from the SFDA for the manufacturing of three new products: **Leigongtengduodai Tablets (雷公滕多苷片)**, an immunosuppressive drug, **Qinghuo Yangyuan Capsules (清火養元膠囊)**, for eliminating heat and detoxifying, and **Kushen Shuan (苦參栓)**, for curing gynecological vaginitis.

Currently, the Group has 9 new pharmaceutical products in the pipeline. The SFDA has given clinical trial approval for **Fu Shu Le Tablets (婦舒樂片)**, for curing gynecological atrophic vaginitis, **Secmidazole Tablets and Capsules (塞克硝唑片及膠囊)**, for curing gynecological trichomoniasis and anaerobe, **Etoposide Phosphate (依托泊苷磷酸酯)**, a gynecological Oncology medicine. **Zhitong Jiangu Capsules (止痛健骨膠囊)**, for osteoarticular pain. Other products under development are: **Paclitaxel Injection (紫杉醇注射液)**, an anti-breast cancer medicine, **Huangtengsu Luhuana Injection (黃藤素氯化鈉注射液)**, for curing gynecological infection and urinary tract infection, **Iopromide (碘普羅胺)** and **Ioversol (碘佛醇)**, clinical diagnostic products.

The above products are mainly used in the gynecological area and are expected to be introduced to the market from 2005 onwards.

During the Year, the Group formed a joint-venture company, Tengen Lizhu Biotech Company Limited (天甲麗珠生物科技有限公司) ("**Tengen Lizhu**"), with Livzon Pharmaceutical Biotechnology Company Limited and Tengen Biomedical Company. The purpose of the new company is to engage in the research on the SARS virus with a goal to the development of a SARS vaccine; and preliminary research on the SARS virus has been successfully completed.

PRODUCTION, PROCUREMENT AND OPERATIONS

The Group purchases major herbal materials from local suppliers in Guizhou where supply is ample; the price for these herbal materials is quite stable. All production lines of the Group have been granted GMP certification and the sales and distribution enterprise of the Group have all been granted Good Service Practice ("**GSP**") certification by SFDA.

SALES AND MARKETING NETWORK

The Group has already established a nationwide sales and distribution network in 29 major provinces and municipalities in the PRC. Currently, there are over 3,000 hospitals, nearly 20,000 drugstores and 5,000 supermarkets selling the Group's prescribed drugs and OTC products. A strong force of over 1,000 professional sales representatives is promoting both categories of products for the Group.

MANAGEMENT DISCUSSION AND ANALYSIS

The Group has been building up its OTC sales and marketing capability (on top of our prescription drugs), including recruiting leading managers in this area.

Sales activities carried out will include point-of-sales promotion, community sales promotions, hospital visits, information exchange, clinical samples and participation in activities organised by the Chinese Society of Clinical Oncology (中國抗癌協會臨床腫瘤協作中心).

PROSPECTS

The management team believes that growth can be sustained through the following business initiatives:

1. **Acquiring Guiyang De Chang Xiang Pharmaceutical Company Limited (貴陽德昌祥藥業有限公司) ("DCX")**

   In October 2004, the Group acquired approximately 80.4% equity interest in DCX. DCX has six GMP production lines, a manufacturing area of 70,000 square meters and a plant with an area of approximately 14,000 square meters. DCX possessed over 120 approved pharmaceutical numbers, 21 of which are for gynecological and obstetrical medicines and approximately 40 of which are for proprietary protected medicines. DCX, as a continued entity of its predecessors, has a history of over 100 years.

2. **Maintaining a leadership position in Prescription Drugs**

   In order to maintain our leading position in the prescription drugs market, we have to maintain the strong growth momentum of our gynecological oncology products. We have to utilise our nationwide sales and distribution network comprising Kanglai Medicine, Guangdong Qunhe, and Chengdu Hechuang to promote our drugs to more hospitals. We would also have to introduce more gynecology products such as **Fu Shu Le Tablets (婦舒樂片)**, **Secmidazole Tablets and Capsules (塞克硝唑片及膠囊)**, **Etoposide Phosphate (依托泊苷磷酸酯)** and **Zhitong Jiangu Capsules (止痛健骨膠囊)** to strengthen our position in this core business area.

3. **Expanding operations in OTC and feminine medicinal healthcare products**

   Recognising the importance and tremendous potential of the markets of OTC and feminine medicinal healthcare products, the Group will expand these businesses by (i) investing in the feminine medicinal healthcare product brand "**Magic 美即**", which was originally owned by Guangdong Qunhe, is now becoming the best choice of consumers in Beijing, Guangdong, etc, and a rising star amongst OTC products of the Group. Guangdong Qunhe launched two self-developed women's skincare products namely, "**Magic Cryptic Foliage Complex Mask**" **(美即植活素面膜)** and "**Magic Skincare Active Extract/Serum**" **(美即美容護膚品精華素)** in the first half of 2004. These two products are being sold in 13 cities in the PRC; (ii) repackaging and launching **Yeosure** Natural Medicine Lotion directly into OTC market, to leverage on its strong hospital brand heritage; and (iii) expanding **Hoholan** and **Huangqi** sales and marketing across the nationwide network.

4. Increasing high-value-added agency

The Group will replace the existing low-value-added trading activities with high-value-added exclusive agency in order to enhance profitability besides increasing our own product sales throughout the sales network.

As a start, in August 2004, the Group signed a Memorandum of Understanding ("**MOU**") with Rockeby biomed Limited, an Australian listed company, to act as its China agent for its leading gynecological diagnosis product, "**CanDia5®**" which is the world's first diagnostic test for vaginal thrush.

5. Focusing on the integration of the Group's resources

The Group continues to focus on the integration of its resources via product portfolio optimilisation; sales and distribution network rationalization (OTC and prescription saleforces separation), and better utilisation of manufacturing centres and human resources.

In order to expand the Group's sales and distribution network in the Hubei Province, the Group has introduced a strategic investor, Wuhan San Tian Trading Company Limited (武漢三田商貿有限公司), which, the management is given to understand, has extensive knowledge in the pharmaceutical market in the Hubei Province and other surrounding provinces, to take up 10% equity interest in Kanglai Medicine from Shenzhen Xinchuang.

The Group will continue to strive to be the leading pharmaceutical enterprise specialising in innovative gynecological medicine and medicinal healthcare products for women in the PRC.

LIQUIDITY AND FINANCIAL RESOURCES

For the Year, the Group generally financed its operations with internally generated cash flows and banking facilities provided by banks in the PRC and Hong Kong. As at 30 June 2004, the Group had cash and bank balances of approximately HK$271.4 million (2003: approximately HK$105.0 million). The gearing ratio (calculated as a ratio of bank loans to shareholders' equity) of the Group as at 30 June 2004 was approximately 34.3%. Net current assets value was approximately HK$402.4 million (2003: approximately HK$190.2 million) and the current ratio was maintained at the healthy level of approximately 3.08 (2003: approximately 2.78) as at 30 June 2004.

The finance costs of the Group for the Year amounted to approximately HK$5.7 million, representing approximately 1.1% of the Group's total turnover and an increase of approximately HK$2.1 million over last year. The increase in finance costs was principally due to new bank loans obtained.

CONTINGENT LIABILITIES

As at 30 June 2004, the Group did not have any material contingent liabilities (2003: Nil).

MANAGEMENT DISCUSSION AND ANALYSIS

BANK BORROWINGS

As at 30 June 2004, the Group had outstanding bank loans of approximately HK$143.0 million from the banks in the PRC and Hong Kong (2003: approximately HK$70.9 million), approximately 60% (2003: approximately 74%) of which were short term bank loans with maturity within one year. All the bank loans of the Group were denominated in Renminbi or Hong Kong Dollar.

As at 30 June 2004, the Group's bank loans were secured by certain (i) plant and machinery of the Group; (ii) land and buildings of the Group; (iii) pledge of fixed deposits; and (iv) corporate guarantee from the Company.

SEASONAL OR CYCLICAL FACTORS

During the Year, the Group's business operations were not significantly affected by any seasonal and cyclical factors.

FOREIGN EXCHANGE EXPOSURE

During the Year, the Group mainly earned revenue and incurred costs in Renminbi. Renminbi was relatively stable during the Year. The Directors considered that the Group's exposure to fluctuation in foreign exchange rate was minimal, and, accordingly, the Group did not employ any financial instruments for hedging purposes.

TREASURY POLICIES

During the Year, the Group generally financed its operations with internally generated resources and credit facilities provided by banks in the PRC and Hong Kong. Interest rates of most of these were calculated by reference to the PRC and Hong Kong bank rates. Both bank deposits and borrowings were mainly denominated in Renminbi or Hong Kong Dollar.

COMMITMENTS

As at 30 June 2004, the Group had contracted commitments of HK$3.0 million (2003: HK$3.1 million) in respect of purchases of technical knowhow.

FINAL DIVIDEND

The Board recommends the payment of a final dividend of HK2 cents per share by the Company for the Year.

MANAGEMENT DISCUSSION AND ANALYSIS

USE OF PROCEEDS FROM NEW ISSUE

The net proceeds from the placing and public offer of new Shares by the Company in December 2002 ("**New Issue**") amounted to approximately HK$54.8 million, of which HK$48.5 million were applied before 30 June 2003 and fully explained in the annual report for the year ended 30 June 2003. During the Year, the Group had utilised the remaining HK$6.3 million as follows:

- approximately HK$1.3 million for the Group's research and development centre and relocation of the Group's head office in the PRC;

- approximately HK$3.0 million for the establishment of 10 sales offices in the PRC to expand the Group's sales and distribution network; and

- for the remaining HK$2.0 million which originally planned for, investing in a joint venture with a pharmaceutical company in Hong Kong for the manufacture and sale of products developed by the Company in the PRC as set out in the Prospectus, as the letter of intent lapsed during the Year, the proceeds of HK$2.0 million are retained and used as working capital of the Group.

EMPLOYEES TRAINING AND REMUNERATION POLICIES

As at 30 June 2004, the Group had a total of 1,024 (2003: 671) (the staff of Chengdu Hechuang was not included in 2003 as it was acquired in June 2003) employees, of whom 1,017 were based in the PRC, with the rest in Hong Kong. The employees of the Group were remunerated based on their experience, qualifications, the Group's performance as well as market conditions. During the Year, staff costs (including director's emoluments) amounted to approximately HK$13,630,000 (2003: HK$7,126,000). Staff costs remained stable at 2.7% of the Group's turnover. The Group participated in retirement benefit schemes for its staff in both Hong Kong and the PRC.

The Group has developed its training programmes in a structured and systematic manner for its management and employees. The Group provided regular management and technical related courses to its employees during the Year.

SHARE OPTION SCHEME

The Company operates a share option scheme ("**Scheme**") for the purpose of providing incentives and/or rewards to eligible participants who contribute to the success of the Group's operations. The Scheme became effective on 25 November 2002, and unless otherwise cancelled or amended, will remain in force for a period of 10 years from that day.

No options were granted under the Scheme during the Year. No option lapsed or was cancelled during the Year. As at 30 June 2004, options carrying the rights to subscribe for 54,850,000 shares in the Company were outstanding.