

## CHAIRMAN'S STATEMENT

Dear Shareholders,

On behalf of the Board of Directors (the "Board"), I am pleased to report a profitable year ended 31 December, 2006 for the Group.

### RESULTS

During the year under review, the Group recorded revenue from continuing operations of approximately HK\$734.65 million, about 2.8% lower than last year. Profit attributable to the Group from continuing operations amounted to approximately HK\$141.17 million, representing an increase of around 29.6% from that of last year before fair value adjustment for derivative financial instrument and also representing an increase of 231% from that of last year after fair value adjustment for derivative financial instrument. Basic earnings per share from continuing operations were approximately HK6.24 cents. The Group launched Mingzheng capsules in July 2006 and Tianqingning injections in November 2006, both of which have great potentia. The new products accounted for approximately 26.7% of the Group's total revenue. The Group had cash equivalents and bank balance of approximately HK\$1,684.16 million. The Group recorded satisfactory performance in spite of the challenging industry environment because it had excellent guidance from the Board and the full support of staff dedicated to following the Group's management concept of "achieving results and containing crisis". The concept is especially crucial to enhancing the Group's competitiveness with the industry changing and the market standardizing. Also, coupled by the "people-oriented and appointment on merit" principle and the belief in "possibility lies in unity",



Mr. Tse Ping, *Chairman*

and employing a result-linked job appraisal system, the Group has created a close association between individual performance with its development. This association has prompted staff to apply their greatest creativity to help the Group achieve the best results.

### DIVIDEND

The Board has recommended the payment of a final dividend of HK2 cents per share, subject to the approval of shareholders at the Annual General Meeting to be held on 18 June, 2007. The final dividend, together with the first quarter dividend of HK1 cent per share, the interim dividend of HK1 cent per share and the third quarter dividend of HK1 cent per share, the total dividend paid for the year 2006 amounted to HK5 cents per share (2005: the total dividend paid was HK11.5 cents per share). The Register of Members of the Company will be closed from Thursday, 14 June, 2007 to Monday, 18 June, 2007, both days inclusive, during which period no transfer of share of the Company will be effected. In order to qualify for the final dividend, all transfers accompanied by the relevant share certificates must be lodged with the Company's branch share registrar, Tengis Limited, 26th Floor, Tesbury Centre, 28 Queen's Road East, Wanchai, Hong Kong by 4:00 p.m. on Wednesday, 13 June, 2007.

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All members of the Board

## INDUSTRY OVERVIEW

### Pharmaceutical Industry

The global pharmaceutical industry grew approximately 6% in 2006, with total value reaching approximately US\$603.7 billion. Market focus continued to shift from the United States of America ("USA") to emerging markets, with PRC boosting the fastest growth among all the biggest medicine markets in the world. Multinational pharmaceutical companies continued to derive drive for profit growth from new and innovative medicines. However, research and development ("R&D") of new medicines is facing increasingly tough barriers including rising costs, more stringent approval processes resulting from withdrawal of medicines with safety issues, and the surge in generic medicines. The low prices of generic medicines have bred a lucrative market that even multinational enterprises find attractive. Branded generic medicines are expected to be major beneficiaries in this competition. More and more multinational enterprises have flocked to the PRC to invest in pharmaceutical production of proprietary medicines, and set up R&D departments in the country. This shows that the PRC pharmaceutical market has strong appeal for global enterprises.

In 2006, pharmaceutical industry in the PRC in terms of production volume and commercial sales continued to grow, while a setback was experienced in the industry profitability. Both import and export surged notably while enterprises suffered bigger losses. Sales growth at the end market (hospitals) recorded the lowest in 10 years while retail sales showed steady growth. As indicated

in the "Economic Analysis of Operation of Pharmaceutical Industry in 2006" by the PRC's National Development and Reform Commission, the total production value of the pharmaceutical industry was RMB553.7 billion, representing an increase of 18.4% against that of last year. Sales income of the pharmaceutical industry was RMB526.8 billion, 19.4% higher than last year. Total profit of industrial enterprises increased by 11.1% to reach RMB41.3 billion. The ratio of sales to production was 95.4%, 0.8% higher than last year. The industrial profit margin was 7.9%, 6.4% lower as compared with last year.

In 2006, the PRC government for the first time included the concern of "difficult and expensive medical care" into its work report. Determination of the government to establish a sustainable and fair medical and health system has brought the pharmaceutical industry into the spotlight. 2006 was also a critical year for the pharmaceutical industry going through adjustment, consolidation and standardization. The PRC government is determined to regulate and standardize market practices, production and new medicine registration, and clamp down on corruption in the industry. Since reformation on the usage of medicines in hospitals was the main focus of government policies, not only sales of existing prescription medicines were affected, marketing of new prescription medicines also became more difficult. The government has been active in tracing and monitoring and conducting unannounced inspection on GMP implementation status of different medicines in order to effectively regulate and standardize medicine production procedures. Furthermore, with the government exercising more caution on of new drug approval and implementing thorough inspection of all registrations and applications to regulate and standardize the R&D and registration procedures of medicines, fewer new medicines were launched during the year. The amended "Guidance for Administration of Medicine Registration" to be launched soon compiled with the principles of "strict definition of new medicines, scientific categorization and management, encouraging proprietary development and innovation, and regulating replication". Aiming at guiding the industry towards a healthy growth path, in addition to implementing different regulatory policies, the government still encourages enterprises to develop innovative products.

## CHAIRMAN'S STATEMENT

The three rounds of price cut measures of medicines last year squeezed the industry's overall profitability. Other market factors such as patents expiry and surfacing of generic medicines also induced intense competition in the market which in turn forced price cuts among indigenous medicines. Those and the increase in water, electricity and gas costs, together with the promulgation of the 2005 PRC "Pharmacopoeia" to raise product quality all led to the increased operation and production costs for pharmaceutical enterprises. Other developments that have aggravated competition included regulation on direct sale, stringent pharmaceutical categorization and centralization of more medicine wholesale companies in the market. Pharmaceutical organizations subject to purchasing through centralized tendering and online tendering for the purpose of enhancing transparency of medicine circulation also posed pressure on margins and profits. Within the industry, mergers and restructuring have been taking place in a more rational manner. As production increases, the market becomes more centralized, and well-known brands continue to gain prominence in the market. It would be the sizeable and stronger players who stand to benefit.

The pharmaceutical industry continues to be a growing industry. As the pharmaceutical market in the PRC is still at the stage of steady growth, players are opened to both challenges and opportunities. Driven by continuous development of the Chinese economy, increasing level of medicine consumption per capita, the growing population and the aging trend, hastening urbanization of rural areas, the country's medical system reform, the development of the community medical system as well as the enlarging coverage of new rural cooperation medical system, the country's pharmaceutical market will expand continuously.

### Coal into Olefin Industry

The coal to olefin industry refines coal into methanol to low carbon olefin products. Low carbon olefin products mainly refer to ethylene and propylene. They are important raw materials for producing organic petroleum. Their end products are widely used in the packaging, construction, textile and pharmaceutical industries. Ethylene industry is a crucial benchmark for measuring a country's level of economic and social sophistication and integrated

strengths. Currently, naphtha is the main raw material for producing low carbon olefin products. China has changed from an oil exporting country into an oil importing country. In 2005, China imported over 40% of its petroleum from overseas. Imported petroleum is expected to make up 60% of all supply in the country by 2020. China has taken over Japan to become the world's second largest oil consumption country (after the USA). With global petroleum reserve dwindling, exploring cost effective non-petroleum raw material for producing low carbon olefin products is of vital importance in helping to ease the threats of petroleum shortage. "Rich in coal, lack of oil with scarce gas" summarizes energy resources distribution in China. Shaanxi, Shanxi and Inner Mongolia are the main regions where coal can be found. If carbon olefin projects were set up close to coal mines, the production cost of low carbon olefin products would be comparable to using naphtha as raw material with petroleum price at US\$30 a barrel. Petroleum price is currently standing at more than US\$50 a barrel and is unlikely to come down in the near future. Thus, refining coal into low carbon olefin products is an effective substitute to using naphtha as the raw material. It has competitive cost, which agrees with China's energy strategy and direction of industrial development.

## OUTLOOK AND PROSPECT

The Group will continue to pursue dual business direction in the pharmaceutical and coal into olefin businesses with utmost diligence. Using profits generated from the pharmaceutical business and abundant capital reserves, the Group plans to:

### 1. Explore potential within the Group

Although the pharmaceutical industry in the PRC will continue to consolidate and standardize, it is still a growth industry. It is believed that the pharmaceutical market will grow steadily and present players with both challenges and opportunities. The continuously booming Chinese economy, improving living standard of the people, increasing average medicine consumption level, the growing Chinese population and the aging trend, hastening urbanization of rural areas, deepening medical system reform, the development of community medical system and the

enlarging coverage of new urban medical system are all driving forces for the pharmaceutical industry. The Group will continue to apply modernized Chinese medicinal technology and biotechnology to research, develop and manufacture medicines that address market needs. It will continue to focus on special treatment areas and develop relevant products and specialty brands to further enhance the Group's competitive advantage. In addition to hepatitis medicines and cardio-cerebral medicine lines, the Group will actively develop oncology medicines, analgesic medicines, respiratory system and anti-diabetic medicines. To accelerate business development, the Group will also continue to launch blockbuster drugs to address market needs and capture market share so as to lower the Group's operating costs and increase the profit margin.

### **2. Accelerate the step of mergers, acquisitions and restructuring of the pharmaceutical companies**

With consolidation and regulation of production, medicine registration and market circulation, pharmaceutical industry in the PRC is encountering dramatic changes. Opportunities and challenges exist in the enhancement of merger and acquisition, R&D capabilities, management skills, end market share and branding. A tendency of more centralized production and market will be seen in the future. With a strong reputation and profound investment management experience in the PRC pharmaceutical industry and abundant capital reserve, the Group has attracted merger and acquisition proposition from a number of large domestic and international enterprises in and outside the country. The Group believes through such deals, it will be able to establish new income streams, develop its business in strong strides and reinforce its industry leadership.

### **3. Invest in and develop the coal into olefin business**

In view of currently high petroleum prices, the Group believes that producing olefin using lower priced coal will help establish a low cost supply

channel for the coal into olefin industry. This is set to bring stable and promising returns to industry players while becoming another income stream for the Group in the long run.

The Group reported outstanding sales and profit with a CAGR of 16% and 33% respectively over the past five years. In addition, it has been among the top 100 enterprises in the PRC's pharmaceutical industry in terms of profitability over the past five years. The Group was also included among the "one of the Best Enterprises under a US Billion within the Asia Pacific Region in 2005" by Forbes Asia, named as "Hong Kong Outstanding Enterprises 2005" by the Economic Digest and included in the "Red Herring Small Cap 100" list by the Red Herring Magazine and was awarded "Chinese Outstanding Enterprise Achievement Prize" by the Capital Magazine in May 2006. These accolades are a testament to outstanding leadership by the Group's management team and the impressive achievements that have resulted. The Group will continue to do its utmost to innovate, increase its market share, reduce the operational cost and enhance returns for shareholders.

### **APPRECIATION**

On behalf of the Board, I would like to express my thanks to our shareholders for their full trust, support and understanding, as well as to all our staff for their contribution and diligence.



**Tse Ping**  
*Chairman*

3 April, 2007