

# MANAGEMENT DISCUSSION AND ANALYSIS

## 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 potential. 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", 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.

## BUSINESS REVIEW

The industry underwent adjustment, consolidation and standardization in 2006 with players including the Group subject to different regulation and market pressures, as stated under the Industry Overview. To combat rising cost, product prices reduction, the difficulties surrounding development of new medicines, and the effects of regulatory measures to bring order into the market and production, the Group looked deeply into the effects posed by industry regulations on its production and operations and made adjustments with reference to its unique characteristics including the nature of its products, its strengths in R&D, brand supremacy, sales network, patented products and technological capabilities. On the internal management front, the Group had its corporate management structure re-organised, improved workflow and redistributed resources, which helped to lower operational cost. It also fine-tuned the product R&D structure to focus more on the development of blockbuster products. The Group also strived to improve profitability by stepping up sales and marketing, brand building and strengthening of its sales network. To boost sales, it mounted more aggressive academic promotion for products with strong potential and injected more resources into developing end-markets and defending market shares. In line with the current medical and health reform, which focuses on the establishment of an effective community health organization for the urban area and rural area correspondingly, the Group also sought to expand the community hospital and retail markets for its medicines and capture every opportunity to promote



JCTT's factory



NJCTT's factory



Beijing Tide's factory

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the enterprise itself and its brands. New promotion channels were established taking into account the unique characteristics of different products. For example, a non-prescriptive medicine (OTC) team was set up to focus on promoting the products to retailers and direct sale via TV channels was used as a means to increase revenue.

On 30 August, 2006, the Company through its wholly-owned subsidiary, CTRC, entered into a joint venture agreement with three companies to establish Shaanxi Xinxing Energy Chemical Industry Limited (陕西新興能源化工有限公司) ("SSEC"). The joint venture is 43%-owned by CTRC, which would contribute RMB752,500,000 as capital of the company. The project was approved by shareholders at the Company's extraordinary general meeting on 12 October, 2006. SSEC is located in Yulin City, Shaanxi Province, the PRC, and will mainly be engaged in the refining of coal into methanol for extracting low carbon olefin (MTO) chemical products, such as ethylene and propylene, and ultimately producing products including polyethylene and polypropylene. Compared with the conventional methods of extracting ethylene and propylene from petroleum, and taking into account the current high price of petroleum, extracting low carbon olefin from cheaper coal has strategic value as a new source of material. Coal into olefin industry is one of the key industries supported by the PRC government. The project is expected to bring stable and promising returns to the Group. Currently, the project is in the pre-construction preparation stage.

For its pharmaceutical operation, the Group will maintain focus on developing specialized medicines where its strengths lie. Apart from boosting its existing medicine series for treating hepatitis and cardio-cerebral diseases,

the Group has also been actively developing analgesic medicines, oncology medicines, respiratory medicines and diabetic drugs, etc.

The Group's principal profit contributors are JCTT, Beijing Tide, Nanjing Chia Tai Tianqing Pharmaceutical Co. Ltd. ("NJCTT") and CTQ.

### **Cardio-cerebral medicines**

Mainly manufactured by Beijing Tide and NJCTT, cardio-cerebral medicines accounted for 21.3% of the Group's turnover. The segment's major product, Kaishi injections, is produced by Beijing Tide. It is based on the Drug Delivery System (DDS) theory and is the first micro-sphere target sustained release medicine in the PRC. This patented technology is championed by Professor Mizushima Yataka, a renowned Japanese medical scientist, and the product has received many national prizes. In recognition of his contribution to the PRC economy, Professor Mizushima was presented the "Friendship Award" and "International Cooperation Award of State Science Technology" by the PRC government. He was further received by China



Chinese Premier Wen Jiabao met with  
Professor Mizushima Yataka



Kaishi injections



Spring PVC-free soft bags  
for intravenous injections



Spring injections



Tianqingnan injections



Tianqingning injections

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national leaders in 2007. Employing advanced technology and boosting high reliable quality, the product is very well received among medical practitioners and patients. Its sales has been rising and, for the year ended 31 December, 2006, reached HK\$310.27 million, making it the best selling product of the Group.

NJCTT and JCTT are engaged in the manufacturing of the Spring PVC-free soft bags for intravenous injections and the Spring injections. Although the Group's Spring PVC-free soft bags for intravenous injections and Spring injections were awarded "Satisfactory and Favorite Quality Brand for Chinese Consumers" in March 2006 by China's Medium-Light Products Quality Assurance Center and are famous for their reliable quality, with Purarin injections under scrutiny by the government for adverse health effects, hospitals have been more cautious in prescribing the medicines. As a result, sales of the two products dropped 40.1% to HK\$30.92 million for the year ended 31 December, 2006.

Tianqinggan injections introduced by NJCTT in April 2004 has been well received by doctors and patients, thereby achieving rapid growth in sales. For the year ended 31 December, 2006, sales of the product amounted to HK\$16.82 million, 51.1% more than that of last year.

Another product with huge potential is NJCTT's Tianqingning injections, which was launched in November 2006. This new product is a plasma-volume expander for patients with blood volume deficiencies. As this product can be used as plasma for all blood types, its wide clinical application is expected to provide huge market potential.

### *Hepatitis medicines*

JCTT is responsible for the R&D and manufacture of hepatitis medicines, which recorded stable sales of HK\$481.71 million for the year ended 31 December, 2006 and accounted for approximately 65.6% of the Group's turnover. In the "People's Safe Medicine Survey" activity jointly organized by Health Times magazine, China Health magazine, Health Digest magazine and People's Health magazine in 2005, the Group's best selling hepatitis drug, Ganlixin, was named a "Safe Medicine for Everyone", speaking volume to the strong recognition it enjoys among medical practitioners and patients for its therapeutic potency.

JCTT is the largest natural herb Licorice's R&D unit and the largest manufacturer of the medicine in China. Hepatitis medicines made with ingredients extracted from Licorice are commonly used in the industry as they are seen as having the best therapeutic effects in protecting the liver and lowering enzyme levels. Ganlixin injections and capsules, Tianqingganping enteric capsules and Tianqingganmei injections are also extracted from Licorice. Ganlixin injections and capsules is the Group's number 1 hepatitis medicine brand and the second largest profit contributor. After the protection period expired for the medicine, many replica products have emerged into the market, resulting in intensified competition and suppressed sales and prices. Overall sales of the product thus dropped slightly to approximately HK\$257.09 million.

As an adequate expedient dosage with good therapeutic effect and intellectual property right protection, Tianqingganping enteric capsules, which was launched in



Ganlixin capsules

Ganlixin injections

Tianqingfuxin  
capsules

Tianqingfuxin  
injections

Tianqingganping  
enteric capsules

Tianqingganmei  
injections

Mingzheng capsules

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May 2004, continued to record persistent sales to reach HK\$53.21 million, a growth of 25.8% when compared with last year. The Tianqingganmei injections, also protected by intellectual property right, is specialized in treating severe hepatitis by lowering enzyme level. Launched in November 2005, it reported strong sales of HK\$17.96 million for the year. The product is expected to quickly become another “blockbuster drug” of the Group.

Extracted and separated from the Chinese Herb called Sophora Alpecuroides L, Tianqingfuxin injections and capsules are the major products for combating the hepatitis virus. Facing intense market competition and pricing pressure, although sales volume increased 24.7% to last year, sales of the product dropped slightly during the year and totaled at approximately HK\$97.25 million. However, as this product is hailed as the number 1 brand of modernized Chinese medicine for fighting hepatitis virus, the Group has full confidence in its prospect.

The Group launched a new patented hepatitis medicine called Mingzheng capsules on 12 July, 2006. A first-tier medicine for combating hepatitis virus in the international market, the product is well received by the market after it was launched. In the latter half year of 2006, its sales reached HK\$29.27 million. The Group is very optimistic about the prospect of the product and believes it will become another blockbuster.

JCTT continues to focus strategically on developing the market for the Group's two major hepatitis medicines for liver protection and combating hepatitis virus and to build a strong brand in the two therapeutic areas.

### ***Oncology medicines***

The Group's oncology medicines are mainly developed

and manufactured by JCTT and NJCTT. They include mainly Tianqingyitai injections and Renyi injections, accounted for 4.8% and 0.6% of the Group's turnover respectively. When it was launched in January 2005, Tianqingyitai injections immediately attracted the attention of medical practitioners and patients. Its sales has been consistently on the rise since then to approximately HK\$35.18 million during the year under review, representing a year-on-year increase of 29.2%. With oncology medicines gaining more significance in its product profile, the Group has established a sales team to promote them.

### ***Analgesic medicines***

In 2005, the Group launched a product line of analgesic medicines, among which the major product is Kaifen injections – the Flurbiprofen Axetie micro-sphere target sustained release analgesic injection, manufactured by Beijing Tide. Produced based on the DDS theory and enabled by advanced target technology, the product is famous for strong pain relieving effect with minimal side effects and has been well received by medical practitioners. The product has been on the growth path since it was launched two years ago. Although analgesic medicines are highly regulated, sales of the product for the year ended 31 December, 2006 still grew to reach approximately HK\$15.22 million, 329.3% higher than the amount achieved in the first year after launch.



Kaifen injections

### ***Diabetic medicines***

The Group's diabetic medicines are manufactured by JCTT. The main product in this category for lowering





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blood sugar level is Taibai sustained release tablets, which was launched in 2004. After two years' promotion, the product has secured wide market acceptance. For the year ended 31 December, 2006, sales of this product increased to HK\$9.88 million. As a first-tier diabetic medicine in the huge PRC market with more than 30 million diabetics, Taibai sustained release tablets can gradually release the medicine and thus maintain a stable level of blood sugar. The product is expected to record remarkable sales in the future.

### **Drug Dosage Forms**

By dosage forms, the Group's different dosage products are all making expected progress. NJCTT's PVC-free soft bags for intravenous injections are well received by medical practitioners and patients. Other ordinary dosage such as sodium chloride and glucose products, as well as large volume PVC-free soft bags for glucose and sodium chloride injection also achieved an average growth in sales of more than 75.7% against the previous year. The notable growth showed that the Group has the ability to produce the right dosages and products based on market demands. The main dosage forms include small volume injections, capsules, tablets, large volume injections and PVC-free soft bags for intravenous injections, accounted for 33.4%, 30.7%, 2.6%, 10.0% and 10.7% of the Group's sales respectively.

### **RESEARCH AND DEVELOPMENT**

The Group continues to focus R&D efforts on cardio-cerebral, hepatitis, oncology, analgesia, respiratory system, diabetes and digestion system medicines. During the year under review, a total of 65 cases had completed

clinical research, under clinical trial or applying for production approval. The Group received 14 production approvals from the SFDA. Currently, 22 cardio-cerebral medicines, 8 hepatitis medicines, 3 oncology medicines, 1 analgesia medicines, 3 respiratory system medicines and 5 diabetic medicines are being developed. The Group has obtained production approvals for 115 medicines.

The Group undertakes self-development and co-development of innovative drugs, and self-development of generic drugs. To enhance its R&D capabilities and accelerate the product development, the Group fully utilizes the society's R&D resources and conducts joint development projects with local and international R&D institutes. Viewing R&D as the foundation for its future development, the Group has invested HK\$42.06 million, representing 5.7% of sales income in 2006.

The Group places great importance on intellectual right protection created in the R&D process. It diligently resorts to appropriate legal means to protect those rights, such as applying for invention patent, utility models patent and apparel design patents. It also pays attention to protecting its critical technologies so as to strengthen its competitive edges. During the year, the Group had filed 26 invention patent applications, obtained 24 patents and 39 announced invention patents. The Group owns a total of 34 invention patents, 3 utility model patents, 13 apparel design patents and 262 announced invention patents. The Group has also filed 36 product invention patents, one of which was international patent (PCT) application. Among its main patented products that have promising market potentials are the cardio-cerebral medicine Kaishi injections, Tianqingganmei injections and Mingzheng capsules.



NJCTT's production plant  
for PVC-free large volume  
injections



JCTT's capsules  
production line



Beijing Tide's small volume  
injections production line



Production workshop of  
Tianqingganmei injections



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In November 2003, the Group was granted a subsidy by the Innovation and Technology Commission of the Hong Kong SAR Government for a study on genetic engineering medicine for hepatitis jointly conducted with the Hong Kong Polytechnic University. The study is progressing smoothly into the application research stage.

### FORMATION OF A JOINT VENTURE COMPANY

On 30 August, 2006, the Company through its wholly-owned subsidiary, CTRC, entered into a joint venture agreement with three companies to set up SSEC. The new company will be owned 43% by CTRC at a total contribution of RMB752,500,000. SSEC will refine coal into methanol to low carbon olefin (MTO) chemical products including ethylene and propylene in Yulin City, Shaanxi Province, the PRC.

It is the first coal into olefin project in the PRC and will employ several patented production technologies. Its technical specifications and installation scale are certified to be of international leading levels by the Industrial Association of Chinese Petroleum and Chemical Industry. It will enhance to lower cost than the conventional methods of extracting similar products from petroleum. With the current high level of petroleum price, participation in the project will allow the Group to gain from the growing PRC coal into olefin business which has relatively high profitability. It will continuously boost the Group's profitability.

The joint venture proposal was approved by shareholders at the Company's extraordinary general meeting on 12 October, 2006.

### INVESTOR RELATIONS

The Group believes practicing good corporate governance will help to increase transparency of its operation. During the year under review, the Group had arranged various press conferences and investors presentations to keep analysts and fund managers up to date with the latest development of the Group. It also participated in different investor roadshows last year, including the CLSA China Forum, UBS Asian

Healthcare Day and Goldman Sachs China Investment Frontier. In addition, the management had meetings with fund managers and analysts regularly to provide them with the latest information of the Group and strengthen investor relations. The Group also posts its annual and interim report, quarterly, interim and annual results announcements, disclosure and circulars on the Company website and the website of The Stock Exchange of Hong Kong Limited. Its aim is to maintain a high degree of transparency in relation to all disclosure of financial and other information.

### CODE ON CORPORATE GOVERNANCE PRACTICES

In the opinion of the Directors, the Company had complied with all the Code Provisions set out in the Code on Corporate Governance Practices as set out in Appendix 14 of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the "Listing Rules") for the year ended 31 December, 2006 with the exception of the following deviations:-

1. Code Provision A.2.1 – The Code Provision stipulates that the roles of chairman and chief executive officer should be separate and should not be performed by the same individual. Mr. Tse Ping is the Chairman and Chief Executive Officer of the Company. The board of Directors (the "Board") considers that Mr. Tse Ping's substantial experience in the pharmaceutical business and management will enhance the Company's decision making and operational efficiency. To help achieve a better balance of power and authority, the Chairman discusses important issues and decisions relating to the Group's business with other Executive Directors.
2. Code Provision E.1.2 – The Code Provision provides that the Chairman of the Board should attend the annual general meeting of the Company. Due to unexpected business commitment, Mr. Tse Ping, the Chairman of the Board, was unable to attend the annual general meeting of the Company held on 5 June, 2006. Mr. Tse Hsin, an Executive Director, was elected in accordance

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with the Company's Articles of Association to act as the chairman of the annual general meeting and together with other Directors present at the meeting, answered questions at the annual general meeting.

### MODEL CODE FOR SECURITIES TRANSACTIONS BY DIRECTORS

The Company has adopted a code of conduct regarding securities transactions by Directors as set out in Appendix 10 of the Listing Rules (the "Model Code"). Having made specific enquiry of all Directors, it was confirmed that all Directors have complied with the required standard set out in the Model Code and the code of conduct regarding securities transactions by Directors adopted by the Company.

### 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 disposal of Sino Concept Technology Limited. As at 31 December, 2006, the Group's bank balance and cash in hand was approximately HK\$1,684.16 million (2005: approximately HK\$1,696.01 million).

### CAPITAL STRUCTURE

As at 31 December, 2006, the Group did not have any loan (2005: Nil).

### CHARGE ON ASSETS

As at 31 December, 2006, the Group did not have any charges on assets (2005: Nil).

### CONTINGENT LIABILITIES

As at 31 December, 2006, the Group had contingent liabilities of HK\$8,464,000 (2005: HK\$4,970,000).

### ASSETS AND GEARING RATIO

As at 31 December, 2006, the total assets of the Group

amounted to approximately HK\$2,215.11 million (2005: approximately HK\$2,140.22 million) whereas the total liabilities amounted to approximately HK\$183.61 million (2005: approximately HK\$164.98 million). The gearing ratio (total liabilities over total assets) was approximately 8.3% (2005: approximately 7.7%).

### EMPLOYEE AND REMUNERATION POLICIES

As at 31 December, 2006, the Group had about 2,694 (2005: 2,546) employees. 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\$128,839,000 (2005: HK\$154,312,000).

### EXPOSURE TO FLUCTUATIONS IN EXCHANGE RATES

Most of the assets and liabilities of the Group were denominated in Renminbi, US dollars 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 exchange rate of HK dollars and US dollars is pledged under the fixed linked system over a long period of time. The Directors consider that the Group is not significantly exposed to foreign currency risk and no hedging or other alternatives have been implemented.