

REPORT OF THE DIRECTORS

The Board present their report together with the audited financial statements for the year ended 31 December 2006.

PRINCIPAL ACTIVITIES

The principal activity of the Company is investment holding and the activities of its subsidiaries are set out in note 9 to the financial statements.

RESULTS

The results of the Group for the year are set out in the consolidated income statement on page 40.

DIVIDEND

An interim dividend of HK\$0.07 per share, amounting to HK\$20,355,000 was declared to the shareholders on 1 September 2006.

The Directors recommend the payment of a final dividend of HK\$0.07 per share, amounting to HK\$20,335,000. The final dividend is subject to approval by the shareholders at the annual general meeting to be held on 23 May 2007 and payable on 22 June 2007.

Interim dividend and recommended final dividend in aggregate, amounting to HK\$40,670,000 or HK\$0.14 per share, are equal to approximately 48% of profit attributable to equity holders of the Company for the year ended 31 December 2006.

RESERVES

Details of movements in the reserves of the Group and of the Company during the year are set out in note 18 to the financial statements.

PROPERTY, PLANT AND EQUIPMENT

Details of the movements in property, plant and equipment of the Group and of the Company during the year are set out in note 7 to the financial statements.

SHARE CAPITAL

Details of the movements in share capital of the Company during the year are set out in note 17 to the financial statements.

REPORT OF THE DIRECTORS

DISTRIBUTABLE RESERVES

Reserves of the Company as at 31 December 2006 available for distribution amounted to RMB21,528,000 (2005: RMB54,426,000). The Company's share premium account in the amount of RMB121,239,000 (2005: RMB121,239,000) is also available for distribution to shareholders, subject to the condition that no distribution or dividend may be paid to shareholders out of the share premium account unless, immediately following the date on which the distribution or dividend is proposed to be paid, the Company shall be able to pay its debts as they fall due in the ordinary course of business.

PRE-EMPTIVE RIGHTS

There is no provision for pre-emptive rights under the Company's articles of association or the laws of the Cayman Islands, which would oblige the Company to offer new shares on a pro-rata basis to existing shareholders.

PURCHASE, SALE OR REDEMPTION OF SECURITIES

The Company has not redeemed any of its Shares during the year. Neither the Company nor any of its subsidiaries has purchased or sold any of the Company's listed securities during the year.

SUBSTANTIAL INVESTMENT AND ACQUISITION

On 23 June 2006, the Group completed the acquisition of 20% of Xi'an Lijun from Rejoy Group Limited Liability Company (the "Rejoy Group") for a consideration of RMB102,556,000. Xi'an Lijun became a wholly-owned subsidiary of the Group after the acquisition. Details of the acquisition had been set out in the circular to the shareholders dated 5 June 2006.

SHARE OPTION SCHEME

Pursuant to a share option scheme approved by a written resolution of all shareholders of the Company on 16 October 2005 ("Scheme"), the Company may grant options to, amongst others, the directors or employees of the Company or its subsidiaries, for the recognition of their contributions to the Group, to subscribe for the Shares. The offer for grant of options ("Offer") must be taken up within 28 days from the date of Offer, with a payment of HK\$1.00 as consideration for the grant. The exercise price of the share option will be determined at the higher of (i) the average closing prices of Shares as stated in the Stock Exchange's daily quotations sheets for the five trading days immediately preceding the date of Offer; (ii) the closing price of Shares as stated in the Stock Exchange's daily quotations sheet on the date of Offer; and (iii) the nominal value of the Shares. The share options are exercisable at any time during a period of not more than 10 years from the date of Offer, subject to the terms and conditions of the Scheme and any conditions of grant as may be stipulated by the Board. Unless terminated by the Company by resolution in general meeting, the Scheme shall be valid and effective for a period of 10 years commencing on the date on which the Scheme becomes unconditional.

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The maximum number of Shares which may be issued upon exercise of all outstanding options granted and yet to be exercised under the Scheme and any other schemes shall not exceed 30% of the issued share capital of the Company from time to time. The total number of Shares which may be issued upon exercise of all options to be granted under the Scheme and any other schemes must not, in aggregate, exceed 10% of the number of Shares in issue as at the date dealings in the Shares first commence on the Stock Exchange unless further shareholders' approval has been obtained pursuant to the conditions set out in the Scheme. The total number of Shares issued and to be issued upon exercise of all options granted under the Scheme and any other schemes (including both exercised or outstanding options) to each participant in any 12-month period shall not exceed 1% of the issued share capital of the Company.

No option has been granted by the Company under the Scheme since its adoption.

DIRECTORS

The Directors during the year were:

Executive Directors

Mr. Wu Qin	(appointed on 27 December 2004)
Mr. Wu Zhihong	(appointed on 27 December 2004)
Mr. Huang Chao	(appointed on 27 December 2004)
Mr. Xie Yunfeng	(appointed on 27 December 2004)
Ms. Sun Xinglai	(appointed on 27 December 2004)
Mr. Wang Xian Jun	(appointed on 22 September 2006)

Non-executive Directors

Mr. Liu Zhiyong	(appointed on 27 December 2004)
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Independent Non-executive Directors

Mr. Qu Jiguang	(appointed on 16 October 2005)
Mr. Leung Chong Shun	(appointed on 16 October 2005)
Mr. Chow Kwok Wai	(appointed on 16 October 2005)

Pursuant to Article 87 of the Company's articles of association, at every annual general meeting one-third of the directors for the time being (or if their number is not three or a multiple of three, the number nearest to but not less than one-third) shall retire from office by rotation and every retiring director shall be eligible for re-election. Accordingly, Mr. Xie Yunfeng, Ms. Sun Xinglai and Mr. Liu Zhiyong will retire from office by rotation in the forthcoming annual general meeting and, being eligible, offer themselves for re-election.

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Furthermore, pursuant Article 86 of the Company's articles of association, any director appointed as an addition to the existing Board shall hold office until the next following annual general meeting of the Company, and shall then be eligible for re-election at that meeting. Accordingly, Mr. Wang Xian Jun will hold office only until the forthcoming annual general meeting and, being eligible, offer himself for re-election.

At the forthcoming annual general meeting, an ordinary resolution will be proposed to re-elect Mr. Xie Yunfeng, Ms. Sun Xinglai and Mr. Wang Xian Jun as executive directors and Mr. Liu Zhiyong as non-executive director.

The Company has received from each of the independent non-executive Directors an annual confirmation of his independence pursuant to Rule 3.13 of the Rules Governing the Listing of Securities on the Stock Exchange ("Listing Rules") and considers the independent non-executive Directors to be independent.

DIRECTORS' SERVICE CONTRACTS

Each of the Directors has entered into a service agreement with the Company for an initial term of 3 years commencing from the appointment date.

Save as disclosed above, none of the Directors has entered into a service contract with the Company which is not determinable by the Company within one year without payment of compensation other than statutory compensation.

DIRECTORS' INTERESTS IN CONTRACTS

Save as disclosed under the heading "Connected transactions", no contracts of significance in relation to the Group's business to which the Company, its holding company or any of its subsidiaries and fellow subsidiaries was a party and in which a director of the Company had a material interest, whether directly or indirectly, subsisted at the end of the year or at any time during the year.

DIRECTORS' RIGHTS TO ACQUIRE SHARES

Apart from the Scheme disclosed above, at no time during the year was the Company, its holding company or any of its subsidiaries and fellow subsidiaries a party to any arrangement to enable the Directors, their respective spouse or minor children to acquire benefits by means of the acquisition of shares in, or debentures of, the Company or in any other body corporate.

EMPLOYEES AND REMUNERATION POLICY

Emoluments of the directors are determined by the Board with reference to the prevailing market practice, the Company's remuneration policy, duties and responsibilities of the Directors within the Group and their contribution to the Group.

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As at 31 December 2006, the Group had 2,300 employees, most of whom were members of the Group's production team based in the PRC. The number of workers employed by the Group varies from time to time depending on its needs and the emolument policy of employees is based on industry practice.

The remuneration policy of the Group's employees are periodically reviewed. Apart from social insurance and in-house training programmes, discretionary bonuses and share options may be awarded to employees according to the assessment of individual performance.

The total remuneration cost incurred by the Group for year ended 31 December 2006 was RMB96,806,000 (2005: RMB87,408,000).

RETIREMENT BENEFIT PLANS

As stipulated by the rules and regulations in the PRC, the Group has participated in state-sponsored defined contribution retirement plans for its employees in the PRC. The Group and the eligible employees are required to contribute 20% and 7%, respectively, of the employees' basic salary. The state-sponsored retirement plans are responsible for the entire pension obligations payable to retired employees. Moreover, the Group would pay monthly allowance to old retired persons. The Group has no further pension obligation beyond the above contributions. Expenses incurred by the Group in connection with the retirement benefit plans were approximately RMB12,036,000 for the year ended 31 December 2006 (2005: RMB9,912,000).

In Hong Kong, the Group has set up a retirement scheme in accordance with the mandatory provident fund requirements prescribed by the Mandatory Provident Fund Schemes Ordinance, Chapter 485 of the Laws of Hong Kong. All Hong Kong based employees and the Group are required to contribute 5% of their respective monthly wages (up to a maximum contribution of HK\$1,000 by each of the employee and the Group) on a monthly basis to the fund.

DIRECTORS' AND CHIEF EXECUTIVES' INTERESTS IN THE SHARES

As at 31 December 2006, the interests of the Directors in the share capital of the Company and its associated corporations (within the meaning of Part XV of the Securities and Futures Ordinance ("SFO")) as recorded in the register required to be kept by the Company pursuant to section 352 of the SFO, or as otherwise notified to the Company and the Stock Exchange pursuant to the Model Code for Securities Transactions by Directors of Listed Issuers ("Model Code") in the Listing Rules once the Shares are listed, were as follows:

Long positions in the Shares

Name of Director	Capacity	Number of shares held	% of the issued share capital of the Company
Mr. Wu Qin	Interest in a controlled corporation (Note)	22,344,000	7.69%

Note: These Shares were registered in the name of and beneficially owned by Success Manage International Limited ("Success Manage"), the issued share capital of which is held as to approximately 37.88% by Mr. Wu Qin. Pursuant to Part XV of the SFO, Mr. Wu Qin is deemed to be interested in all the Shares held by Success Manage. These Shares has been pledged to Guotai Junan Securities (Hong Kong) Limited.

REPORT OF THE DIRECTORS

Save as disclosed above, as at 31 December 2006, none of the Directors or chief executives had an interest or short position in the Shares, underlying shares or debentures of the Company or any of its associated corporations that was required to be recorded pursuant to Section 352 of the SFO, or as otherwise notified to the Company and the Stock Exchange pursuant to the Model Code.

SUBSTANTIAL SHAREHOLDERS' AND OTHER PERSON'S INTERESTS IN THE SHARES

The register of substantial shareholders required to be kept by the Company under section 336 of the SFO shows that as at 31 December 2006, the Company had been notified of the following interests and short positions, being 5% or more in the issued share capital of the Company. These interests are in addition to those disclosed above in respect of the Directors and chief executives.

Long positions in the Shares

Name of shareholder	Capacity	Number of Shares	% of the issued share capital of the Company
Prime United (Note 1)	Beneficial owner	123,984,000	42.68%
Victory Rainbow Investment Limited	Beneficial owner	58,300,000	20.07%
Grand Ocean Shipping Company Ltd. (Note 2)	Interest of controlled corporation	58,300,000	20.07%
Ms. Chen Lin-Dong (Note 2)	Interest of controlled corporation	58,300,000	20.07%
Mr. Xu Ming (Note 2)	Interest of controlled corporation	58,300,000	20.07%
Success Manage	Beneficial owner	22,344,000	7.69%
Mr. Wu Qiu (Note 3)	Interest of controlled corporation	22,344,000	7.69%
Ms. Zhang Mingfang (Note 3)	Interest of spouse	22,344,000	7.69%
Guotai Junan Securities Co., Ltd. (Note 3)	Person having a security interest in shares	22,344,000	7.69%
Japan Trustee Services Bank, Ltd	Trustee	15,016,000	5.17%

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SUBSTANTIAL SHAREHOLDERS' AND OTHER PERSON'S INTERESTS IN THE SHARES *(Continued)*

Notes:

1. Prime United is held as to 2.43% by Mr. Wu Qin, an executive Director, as to approximately 2.43% by Mr. Wu Zhihong, an executive Director, as to approximately 2.41% by Mr. Huang Chao, an executive Director, as to approximately 4% by Mr. Xie Yunfeng, an executive Director, as to approximately 4% by Ms. Han Yamei, a member of the management of Xi'an Lijun, and as to approximately 84.73% by Mr. Wu Qin, Mr. Wu Zhihong, Mr. Huang Chao, Mr. Xie Yunfeng and Ms. Han Yamei who jointly hold such shares on trust for 4,965 individuals who are present and former employees or their respective estates of Xi'an Lijun and Rejoy Group. The beneficial ownership structure in Prime United is a replication of the ownership structure of Rejoy Technology.
2. Victory Rainbow Investment Limited is wholly-owned by Grand Ocean Shipping Company Ltd., a company incorporated in the Republic of Liberia, which in turn is owned as to 50% by Ms. Chen Lin-Dong and 50% by Mr. Xu Ming. By virtue of Part XV of the SFO, each of Grand Ocean Shipping Company Ltd., Ms. Chen Lin-Dong and Mr. Xu Ming is deemed to be interested in the Shares held by Victory Rainbow Investment Limited.
3. Success Manage is held as to approximately 37.88% by Mr. Wu Qin. Pursuant to Part XV of the SFO, the spouse of Mr. Wu Qin, Ms. Zhang Minfang, is deemed to be interested in all the Shares held by Success Manage. These Shares has been pledged to Guotai Junan Securities (Hong Kong) Limited.

MANAGEMENT CONTRACTS

Save as disclosed under the heading "Connected transactions", no other contracts concerning the management and administration of the whole or any substantial part of the business of the Group were entered into or in existence during the year.

MAJOR SUPPLIERS AND CUSTOMERS

During the year, the Group purchased less than 30% of its total purchases from its 5 largest suppliers and sold less than 30% of its turnover to its 5 largest customers.

CONNECTED TRANSACTIONS

Certain related party transactions as disclosed in note 34 to the financial statements also fell under the definition of "connected transaction" or "continuing connected transaction" in Chapter 14A of the Listing Rules, details of which are set out below. The Company has complied with the disclosure requirements, where applicable, in accordance with Chapter 14A of the Listing Rules.

(1) Connected transactions

On 23 June 2006, the Company had completed the acquisition from Rejoy Group for the 20% equity interests in Xi'an Lijun. Before the acquisition, Xi'an Lijun was owned as to 80% by the Company and 20% by Rejoy Group. The consideration is RMB102,556,000 which was arrived at after arm's length negotiations between Rejoy Group and the Company. Rejoy Group was a substantial shareholder of Xi'an Lijun, a subsidiary of the Company, and as such Rejoy Group was a connected person of the Company under the Listing Rules. The transfer therefore constituted a connected transaction of the Company for the purpose of the Listing Rules.

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CONNECTED TRANSACTIONS *(Continued)*

(2) Continuing Connected Transaction

(i) *Discontinued Continuing Connected Transaction*

(a) *Lease of land-use rights by Xi'an Lijun from Rejoy Group*

Pursuant to the lease of land-use rights agreement entered into between Xi'an Lijun and Rejoy Group on 16 October 2005 ("Land-Use Rights Agreement"), Xi'an Lijun leased land-use rights from Rejoy Group for a term commencing from 1 July 2005 and ending on 31 December 2007. Particulars of the areas of leased land were set out in the property valuation report in Appendix III to the Prospectus dated 2 December 2005 ("Prospectus"). The total areas of the leased land amounted to approximately 113,768 square metres and the rent paid by Xi'an Lijun was at RMB4 per square metre per month. The Group entered into the Land-Use Rights Agreement as the production plants, storage, office buildings of Xi'an Lijun are located on the relevant land.

Rejoy Group was a connected person of the Company under the Listing Rules as it holds 20% of interests of Xi'an Lijun. On 22 June 2006, the Company had completed the acquisition of 20% interests of Xi'an Lijun from Rejoy Group, and Rejoy Group was therefore no longer a connected person of the Company. For the year ended 31 December 2006, the total amount paid by the Group to Rejoy Group in respect of the land-use rights was approximately RMB5,460,864 (2005: RMB5,460,864), which did not exceed the annual cap of RMB5,460,864 (2005: RMB5,460,864) prescribed for the year ended 31 December 2006 as disclosed in the Prospectus.

(b) *Purchase of packaging materials from Xi'an Global Printing Co., Ltd. (西安環球印務有限公司) ("Global Printing")*

The principal business of Global Printing is printing of packaging materials. The Group had been purchasing packaging materials from Global Printing on an ongoing basis for packaging its own products.

Pursuant to the supply agreement dated 16 October 2005 entered into between Xi'an Lijun and Global Printing, Xi'an Lijun purchased packaging materials from Global Printing for a term of 3 years commencing from 1 January 2005 and ending on 31 December 2007. The Directors confirmed that the purchase prices of packaging materials from Global Printing had been determined in accordance with the market prices and on normal commercial terms, and that the Group had paid to Global Printing for the packaging materials at prices no less favorable than those paid to independent third parties and on terms no less favorable than those the Group could obtain from independent third parties.

Global Printing is connected person of the Company under the Listing Rules as it is held as to 45% by Shaanxi Pharmaceutical Company (陝西省醫藥總公司) ("SPC"), which also holds all the interests in Rejoy Group, a substantial shareholder of Xi'an Lijun. On 22 June 2006, the Company had completed the acquisition of 20% interests of Xi'an Lijun from Rejoy Group, and Global Printing was therefore no longer a connected person of the Company. For the year ended 31 December 2006, the total amount paid by the Group to Global Printing for the purchase of packaging materials amounted to approximately RMB6,636,000 (2005: RMB6,883,000), which did not exceed the estimated annual cap of RMB9,000,000 (2005: RMB8,500,000) prescribed for the year ended 31 December 2006 as disclosed in the Prospectus.

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CONNECTED TRANSACTIONS (Continued)

(2) Continuing Connected Transaction (Continued)

(i) Discontinued Continuing Connected Transaction (Continued)

- (c) *Provision of utilities such as electricity, water, steam, cooling salt water and compressed air by Shaanxi Xi'an Pharmaceutical Factory ("Xi'an Pharmacy Factory")*

Xi'an Pharmacy Factory had been supplying utilities to Xi'an Lijun. Pursuant to the utilities services agreement entered into between Xi'an Lijun and Xi'an Pharmacy Factory on 16 October 2005, Xi'an Pharmacy Factory supplied utilities including electricity, water, steam, cooling salt water and compressed air to Xi'an Lijun for a term of three years commencing from 1 January 2005 and ending on 31 December 2007. The charges for electricity and water payable by Xi'an Lijun were calculated based on the state-prescribed prices (tax inclusive) plus actual processing costs of Xi'an Pharmacy Factory. In respect of steam, cooling salt water and compressed air, such charges were determined based on actual costs of production incurred by Xi'an Pharmacy Factory. The reason for the Group entering into the above agreement was to satisfy the needs of Xi'an Lijun in respect of its production, office and storage.

Xi'an Pharmacy Factory is a connected person to the Company as it is a wholly-owned subsidiary of Rejoy Group, a substantial shareholder of Xi'an Lijun. On 22 June 2006, the Company had completed the acquisition of 20% interests of Xi'an Lijun from Rejoy Group, and Xi'an Pharmacy Factory was therefore no longer a connected person of the Company. For the year ended 31 December 2006, the total amount paid by the Group to Xi'an Pharmacy Factory in respect of supply of utilities amounted to approximately RMB54,032,000 (2005: RMB50,973,000), which did not exceed the estimated annual cap of RMB60,500,000 (2005: RMB55,000,000) prescribed for the year ended 31 December 2006 as disclosed in the Prospectus.

- (d) *Sharing of administrative costs between Xi'an Lijun and Xi'an Pharmacy Factory*

Xi'an Lijun had been sharing the administrative costs of Xi'an Pharmacy Factory so that the employees of Xi'an Lijun were entitled to enjoy certain facilities and services including hospitals, nursery, schools, security, property management and environmental beautification provided by Xi'an Pharmacy Factory. Pursuant to the agreement entered between Xi'an Lijun and Xi'an Pharmacy Factory on 16 October 2005, Xi'an Lijun shared the administrative costs of Xi'an Pharmacy Factory so that the employees of Xi'an Lijun would continue to be able to enjoy the aforesaid facilities and services provided by Xi'an Pharmacy Factory for a term of three years commencing from 1 January 2005 and ending on 31 December 2007. The total amount of administrative costs was based on the actual costs incurred for the provision of the aforesaid facilities and services. The share of administrative costs borne by Xi'an Lijun was determined with reference to the actual number of employees of Xi'an Lijun utilizing such facilities and services.

Xi'an Pharmacy Factory is a connected person to the Company by virtue of being a wholly-owned subsidiary of Rejoy Group, a substantial shareholder of Xi'an Lijun. On 22 June 2006, the Company had completed the acquisition of 20% interests of Xi'an Lijun from Rejoy Group, and Xi'an Pharmacy Factory was therefore no longer a connected person of the Company. For the year ended 31 December 2006, the total amount paid by the Group to Xi'an Pharmacy Factory in respect of the administration costs amounted to approximately RMB13,000,000 (2005: RMB12,926,000), which did not exceed the estimated annual cap of RMB13,000,000 (2005: RMB13,000,000) prescribed for the year ended 31 December 2006 as disclosed in the Prospectus.

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CONNECTED TRANSACTIONS *(Continued)*

(2) Continuing Connected Transaction *(Continued)*

(i) **Discontinued Continuing Connected Transaction** *(Continued)*

- (e) *Distribution of the Group's products by Xi'an Rejoy Medicine Co., Ltd. (西安利君醫藥有限公司) ("Rejoy Medicine")*

Rejoy Medicine has been one of the Group's distributors in Xi'an and is principally engaged in the retail and distribution of pharmaceutical products. Pursuant to the purchase and distribution agreement entered into between Rejoy Medicine and Xi'an Lijun on 16 October 2005, Rejoy Medicine purchased products from Xi'an Lijun and distributed such products to other distributors and end customers for a term of three years commencing from 1 January 2005 and ending on 31 December 2007. The Directors confirmed that the selling prices of the Group's products sold to Rejoy Medicine had been determined in accordance with the market prices and that the Group charged Rejoy Medicine for the products at prices no less favorable than those charged to independent third parties and on terms no less favorable than those the Group could obtain from independent third parties.

Rejoy Medicine is a connected person to the Company as it is held as to 55% by Rejoy Group, a substantial shareholder of the Xi'an Lijun. On 22 June 2006, the Company had completed the acquisition of 20% interests of Xi'an Lijun from Rejoy Group, and Rejoy Medicine was therefore no longer a connected person of the Company. For the year ended 31 December 2006, the Group's sale to Rejoy Medicine amounted to approximately RMB10,154,000 (2005: RMB20,886,000), which did not exceed the estimated annual cap of RMB27,800,000 (2005: RMB27,000,000) prescribed for the year ended 31 December 2006 as disclosed in the Prospectus.

(ii) **Continuing connected transactions**

- (a) *Distribution of the Group's products by Rejoy Baichuan Medicines Chemical Engineering Co., Ltd. ("Rejoy Baichuan")*

Rejoy Baichuan has been one of the Group's distributors in the northwest market of the PRC and is principally engaged in the retail and distribution of pharmaceutical products. Pursuant to the purchase and distribution agreement entered into between Xi'an Lijun and Rejoy Baichuan on 16 October 2005, Rejoy Baichuan purchased products from Xi'an Lijun and distributed such products to other distributors and end customers for a term of three years commencing from 1 January 2005 and ending on 31 December 2007. The Directors confirmed that the selling prices of the Group's products sold to Rejoy Baichuan had been determined in accordance with the market prices and that the Group charged Rejoy Baichuan for the products at prices no less favorable than those charged to independent third parties and on terms no less favorable than those the Group could obtain from independent third parties.

Rejoy Baichuan is held as to 84% by Rejoy Technology, the issued share capital of which is held as to 100% by the beneficial shareholders of Prime United, one of the controlling shareholders of the Company. Accordingly, Rejoy Baichuan is a connected person of the Company under the Listing Rules. For the year ended 31 December 2006, the Group's sales to Rejoy Baichuan amounted to approximately RMB19,515,000 (2005: RMB9,043,000), which did not exceed the estimated annual cap of RMB24,800,000 (2005: RMB24,000,000) prescribed for the year ended 31 December 2006 as disclosed in the Prospectus.

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CONNECTED TRANSACTIONS *(Continued)*

(2) Continuing Connected Transaction *(Continued)*

(ii) Continuing connected transactions *(Continued)*

- (b) *Distribution of the Group's products by Liaoning Huabang Pharmaceutical Co., Ltd. (遼寧華邦醫藥有限公司) ("Huabang Pharmaceutical")*

Huabang Pharmaceutical has been one of the Group's distributors in the northeast market of the PRC and is principally engaged in the retail and distribution of pharmaceutical products. Pursuant to the purchase and distribution agreement entered into between Xi'an Lijun and Huabang Pharmaceutical on 16 October 2005, Huabang Pharmaceutical purchased products from Xi'an Lijun and distributed such products to other distributors and end customers for a term of three years commencing from 1 January 2005 and ending on 31 December 2007. The Directors confirmed that the selling prices of the Group's products sold to Huabang Pharmaceutical had been determined in accordance with the market prices and that the Group charged for the products at prices no less favorable than those charged to independent third parties and on terms no less favorable than those the Group could obtain from independent third parties.

The registered capital of Huabang Pharmaceutical is held as to 100% by the beneficial shareholders of Bondwise Trading Limited, one of the controlling shareholders of the Company. Accordingly, Huabang Pharmaceutical is a connected person of the Company under the Listing Rules. For the year ended 31 December 2006, the Group's did not have any transaction with Huabang Pharmaceutical (2005: RMB4,526,000), the estimated annual cap prescribed for the year ended 31 December 2006 as disclosed in the Prospectus was RMB11,000,000 (2005: RMB11,000,000).

The aforesaid continuing connected transactions have been reviewed by independent non-executive Directors of the Company. The independent non-executive Directors confirmed that the aforesaid connected transactions were entered into (a) in the ordinary and usual course of business of the Group; (b) either on normal commercial terms or on terms no less favourable to the Group than terms available to or from independent third parties; (c) in accordance with the relevant agreements governing them on terms that are fair and reasonable and in the interests of the shareholders of the Company as a whole; (d) have not exceeded the relevant maximum amount capped in accordance to the waiver previously granted by the Stock Exchange.

Based on the work performed, the auditors of the Company have confirmed that the aforesaid continuing connected transaction (a) have been approved by the Board of the Company; (b) have been entered into in accordance with the terms of the relevant agreements governing the transactions; and (c) have not exceeded the caps allowed by the Stock Exchange in the previous waiver.

SUFFICIENCY OF PUBLIC FLOAT

Based on the information that is publicly available to the Company and within the knowledge of the Directors, it is confirmed that a sufficient public float of more than 25% of the issued capital of the Company has been maintained as at 31 December 2006.

REPORT OF THE DIRECTORS

POST BALANCE SHEET EVENTS

On 25 March 2007, the Company entered into an acquisition agreement with CMP Group Limited (the "Vendor") and China Pharmaceutical Company Limited (being the guarantor of the Vendor under the acquisition agreement) to purchase the entire interests in, and a shareholder loan of, New Orient Investments Limited ("New Orient") at a consideration which is equivalent to the aggregate sum of (i) 7.5 times the audited profit attributable to the shareholders of New Orient and its subsidiaries (excluding any profit or loss generated in connection with foreign exchanges) for the year ended 31 December 2006; and (ii) any income generated in connection with foreign exchanges for the year ended 31 December 2006. However, in any event, the consideration shall not exceed HK\$510,000,000.

The Acquisition constitutes a major transaction of the Company under Rule 14.06(3) of the Listing Rules. As Mr. Qu Jiguang is a connected person of the Company and also the ultimate controlling shareholder of the Vendor, the entering into of the Acquisition Agreement constitutes a connected transaction for the Company under Chapter 14A of the Listing Rules. The Acquisition agreement is subject to approval of the Independent Shareholders at the extraordinary general meeting.

MODEL CODE FOR SECURITIES TRANSACTIONS BY DIRECTORS

The Board has adopted a code of conduct regarding Directors' securities transactions on terms no less exacting than the required standard set out in the Model Code for Securities Transactions by Directors of Listed Issuers as set out in Model Code. The Directors confirmed that there were not any non-compliance with the standard set out in the Model Code and the Company's code of conduct regarding Directors' securities transactions during the year ended 31 December 2006.

AUDITORS

The financial statements have been audited by PricewaterhouseCoopers who retire and, being eligible, offer themselves for re-appointment at the forthcoming annual general meeting.

ANNUAL GENERAL MEETING

The 2007 Annual General Meeting of the Company will be held at Salon IV, M/F, Grand Hyatt Hong Kong, 1 Harbour Road, Wanchai, Hong Kong on 23 May 2007 at 11:00 a.m. and the Notice of Annual General Meeting will be published and dispatched in due course.

CLOSURE OF REGISTER OF MEMBERS

The register of members of the Company will be closed from Thursday, 17 May 2007 to Wednesday, 23 May 2007 (both days inclusive) during which period no transfer of Shares will be effected. In order to qualify for the proposed final dividend and the entitlement to attend and vote at the forthcoming annual general meeting, all transfer documents, accompanied by the relevant share certificates, must be lodged with the Company's branch share registrar and transfer office of the Company in Hong Kong, Computershare Hong Kong Investor Services Limited, at Shops 1806-1807, 18th Floor, Hopewell Centre, 183 Queen's Road East, Hong Kong not later than 4:30 p.m. on Wednesday, 16 May 2007.

On behalf of the Board

Wu Qin
Chairman

Hong Kong, 26 April 2007