



年

2006

Annual Report

報



廣州藥業股份有限公司

Guangzhou Pharmaceutical Company Limited

( Stock code : 0874 )

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## 1. IMPORTANT NOTICE

- I. The Board of Directors (the "Board"), the Supervisory Committee (the "Supervisory Committee") of Guangzhou Pharmaceutical Company Limited ("GPC" or the "Company") and its Directors, Supervisors and Senior Management collectively and individually accept full responsibility for the authenticity, accuracy and completeness of the information contained in this report and confirm that there are no false information, misleading statements or material omissions in this report.
- II. Guangdong Yangcheng Certified Public Accountants Co., Ltd., the domestic auditor, and PricewaterhouseCoopers, the international auditor, have audited the financial reports of the Company together with its subsidiaries (collectively the "Group") and the Company for the year ended 31 December 2006 (the "Reporting Period" or the "Year") and issued unqualified auditors' reports thereon.
- III. Mr. Yang Rongming (Chairman of the Board), Mr. Shi Shaobin (Director and General Manager), and Mr. Chen Binghua (Financial Controller and Senior Manager of the Finance Department) individually accept responsibility for ensuring the authenticity and completeness of the financial reports contained in this report.
- IV. This report is prepared in both English and Chinese. In the event that different interpretation occurs, with the exception of the financial reports prepared in accordance with Hong Kong Financial Reporting Standards ("HKFRS") and the international auditor's report thereon, the Chinese version shall prevail.

# Company Profile

- I. Legal Chinese name: 廣州藥業股份有限公司  
Chinese name abbreviation: 廣州藥業  
English name: Guangzhou Pharmaceutical Company Limited  
English name abbreviation: GPC
- II. Legal representative: Yang Rongming
- III. Company secretary: He Shuhua  
Representative of securities affairs: Huang Xuezhen  
Address: 45 Sha Mian North Street, Guangzhou City  
Guangdong Province, the PRC  
Telephone: (8620) 8121 8084/8121 8086  
Fax: (8620) 8121 6408  
E-mail: hesh@gpc.com.cn/huangxz@gpc.com.cn
- IV. Registered address and office: 45 Sha Mian North Street, Guangzhou City  
Guangdong Province, the PRC  
Postal code: 510130  
Internet website: <http://www.gpc.com.cn>  
E-mail: sec@gpc.com.cn  
Principal place of business in Hong Kong: Room 2005, 20th Floor, Tower Two Lippo Center,  
89 Queensway, Hong Kong
- V. Designated newspapers for information disclosure: Mainland China: Shanghai Securities  
Hong Kong: Hong Kong Economic Times  
The Standard
- Internet website designated by the China Securities Regulatory Commission for publishing this annual report: <http://www.sse.com.cn>
- Internet website designated by The Stock Exchange of Hong Kong Limited for publishing this annual report: <http://www.hkex.com.hk>
- Place where this annual report is available for inspection: The Secretariat to the Board of Directors of  
Guangzhou Pharmaceutical Company Limited
- VI. Place of listing, name and codes of the Company's shares: A Shares: The Shanghai Stock Exchange  
Stock Code: 600332 Stock Abbreviation: GZ Phar.  
H Shares: The Stock Exchange of Hong Kong Limited  
Stock Code: 0874 Stock Abbreviation: GZ Phar.
- VII. Other corporate information: First registration date: 1 September 1997  
First place of registration: 45 Sha Mian North Street, Guangzhou City  
Guangdong Province, the PRC  
Registration date for subsequent change: 20 October 2006  
Place of registration for subsequent change: 45 Sha Mian North Street, Guangzhou City  
Guangdong Province, the PRC  
Business registration number: 4401011101830  
Tax registration number: 44010063320680x  
Auditors: International auditor: PricewaterhouseCoopers Certified Public Accountants  
22nd Floor, Prince's Building, Central, Hong Kong  
PRC auditor: Guangdong Yangcheng Certified Public Accountants Co., Ltd.  
25th Floor, Jianlibao Plaza, No. 410  
Dongfeng Zhong Road, Guangzhou 510040,  
Guangdong, PRC



# Financial Data and Financial Highlights

## I. EXTRACTED FROM THE FINANCIAL STATEMENTS PREPARED IN ACCORDANCE WITH PRC ACCOUNTING STANDARDS AND SYSTEMS

Items	2006 (RMB'000)
1 Total profit	370,362
2 Net profit	227,328
3 Net profit after extraordinary non-operating ( <i>note</i> )	226,567
4 Profit from principal operations	1,743,185
5 Profit from other operations	41,508
6 Operating profit	366,753
7 Investment income	7,106
8 Grants and subsidies	1,190
9 Net non-operating income and expenses	(4,686)
10 Net cash inflows from operating activities	38,880
11 Net increase in cash and cash equivalents	(127,855)

Note: Non-operating items

Items	Amount (RMB'000)
Losses on disposal of long-term equity investments and fixed assets	(2,455)
Government grants and subsidies	1,190
Gain/(Loss) from short-term investments	6,025
Non-operating expenses after deducting provision for value impairment of assets	(2,214)
Income/(Loss) of entrusted loans	(1,099)
Income tax effect	(591)
Minority interests	(95)
Total	761

## II. DIFFERENCES BETWEEN THE FINANCIAL STATEMENTS PREPARED IN ACCORDANCE WITH PRC ACCOUNTING STANDARDS AND SYSTEMS AND HKFRS

	As at 31 December 2006 (RMB'000)	As at 31 December 2005 (RMB'000)
Net assets under PRC Accounting Standards and Systems	2,788,088	2,621,437
Intangible assets capitalised	27,006	37,367
Difference arising from fixed assets revaluation	126,547	128,522
Deferred government grants	(3,279)	(4,259)
Difference in provision for employee benefits in medical insurance	(60,197)	(53,586)
Provision for deferred taxation	23,082	10,822
Impairment on goodwill	(1,579)	(1,791)
Revaluation of investment properties	13,105	—
Difference in minority interest	(15,384)	(15,389)
Capital and reserves attributable to equity holders of the Company under HKFRS	<u>2,897,389</u>	<u>2,723,123</u>



# Financial Data and Financial Highlights

## II. DIFFERENCES BETWEEN THE FINANCIAL STATEMENTS PREPARED IN ACCORDANCE WITH PRC ACCOUNTING STANDARDS AND SYSTEMS AND HKFRS (continued)

	For the year ended 31 December 2006 (RMB'000)	For the year ended 31 December 2005 (RMB'000)
Net profit under PRC Accounting Standards and Systems	227,328	184,482
Amortisation of intangible assets	(10,361)	(10,382)
Additional depreciation on revalued fixed assets	(1,975)	(1,975)
Government grants recognised as income	1,106	452
Difference in provision for employee benefits in medical insurance	(6,611)	6,017
Provision for deferred taxation	12,260	4,841
Reversals of amortisation on goodwill/(Impairment on goodwill)	212	(1,791)
Unsettled long outstanding payables written off recognised as income	2,498	2,397
Negative goodwill arising from the additional investment of an external investor in a subsidiary	—	19,819
Negative goodwill arising from investment in an associate	238	—
Donations recognised as income	91	440
Appropriation to staff bonus and welfare fund charged as expenses	(7,680)	(6,074)
Decline in fair value of investment properties	(12)	—
Gain from disposal of fixed assets recognised as income	729	—
Difference in minority interest	244	(422)
Profit attributable to equity holders of the Company under HKFRS	<u>218,067</u>	<u>197,804</u>

## III. PRINCIPAL FINANCIAL DATA AND FINANCIAL INDICATORS

### 1. Financial statements prepared in accordance with PRC Accounting Standards and Systems

Indicators	2006	2005	2004
Income from principal operations (RMB'000)	10,241,004	9,026,340	7,708,314
Net profit (RMB'000)	227,328	184,482	55,292
Total assets (RMB'000)	5,409,413	5,098,095	5,182,878
Shareholders' funds (excluding minority interests) (RMB'000)	2,788,088	2,621,437	2,440,230
Earnings per share (RMB)	0.28	0.23	0.07
Net assets per share (RMB)	3.44	3.23	3.01
Adjusted net assets per share (RMB)	3.41	3.17	2.96
Net cash inflows from operating activities per share (RMB)	0.05	0.18	0.25
Return on net assets (fully diluted) (%)	8.15	7.04	2.27
Return on net assets (weighted average) (%)	8.40	7.31	2.27
Return on net assets from net profit after deducting non-operating items (weighted average) (%)	8.74	7.64	2.63
Ratio of shareholders' funds (excluding minority interests) (%)	51.54	51.42	47.08
Gearing ratio (%) (Note)	45.39	44.94	49.13

Note: Gearing ratio is calculated according to the following formula: total liabilities/total assets x 100%



# Financial Data and Financial Highlights

## III. PRINCIPAL FINANCIAL DATA AND FINANCIAL INDICATORS *(continued)*

### 2. Accounts prepared in accordance with HKFRS

Indicators	2006	2005	2004	2003	2002
Turnover (RMB'000)	<b>10,241,004</b>	9,026,340	7,709,565	6,973,113	5,943,823
Profit before income tax (RMB'000)	<b>349,155</b>	315,493	161,675	307,829	196,360
Profit attributable to equity holders of the Company (RMB'000)	<b>218,067</b>	197,804	42,829	146,667	101,155
Total assets (RMB'000)	<b>5,640,964</b>	5,316,420	5,413,438	4,954,091	4,410,210
Total liabilities (RMB'000)	<b>2,560,584</b>	2,391,590	2,655,559	2,220,047	1,807,058
Capital and reserves attributable to equity holders of the Company (RMB'000)	<b>2,897,389</b>	2,723,123	2,545,592	2,551,417	2,454,080
Earnings per share (RMB)	<b>0.27</b>	0.24	0.05	0.18	0.13
Capital and reserves attributable to equity holders of the Company per share (RMB)	<b>3.57</b>	3.36	3.14	3.15	3.03
Return on capital and reserves attributable to equity holders of the Company (%)	<b>7.53</b>	7.26	1.68	5.75	4.12
Ratio of Capital and reserves attributable to equity holders of the Company (%)	<b>51.36</b>	51.22	47.02	51.50	55.65
Gearing ratio (%) (Note)	<b>45.39</b>	44.98	49.05	44.81	40.97

Note: Gearing ratio is calculated according to the following formula: total liabilities/total assets x 100%

## IV. FINANCIAL INDICATORS AS REQUIRED BY THE INFORMATION DISCLOSURE FOR COMPANIES ISSUING LISTED SECURITIES (NO. 9) PROMULGATED BY THE CHINA SECURITIES REGULATORY COMMISSION (THE "CSRC") (PREPARED IN ACCORDANCE WITH THE PRC ACCOUNTING STANDARDS AND SYSTEMS)

Profit for the Reporting Period	Return on net assets		Earnings per share	
	Fully diluted (%)	Weighted average (%)	Fully diluted (RMB)	Weighted average (RMB)
Profit from principal operations	62.52	64.40	2.15	2.15
Operating profit	13.15	13.55	0.45	0.45
Net profit	8.15	8.40	0.28	0.28
Net profit after deducting non-operating items	8.13	8.74	0.28	0.28





# Financial Data and Financial Highlights

## V. CHANGE IN SHAREHOLDERS' FUNDS DURING THE REPORTING PERIOD IN 2006 (CONSOLIDATED)

### 1. Extracted from the accounts prepared in accordance with the PRC Accounting Standards and Systems

Items	Share capital (RMB'000)	Capital reserve (RMB'000)	Surplus reserve (RMB'000)	Include: statutory public welfare fund (RMB'000)	Retained earnings (RMB'000)	Shareholders' funds (RMB'000)
Opening balance	810,900	1,149,454	567,243	179,462	93,840	2,621,437
Additions	—	3,766	261,755	—	229,215	494,736
Deductions	—	—	180,935	179,462	147,150	328,085
Closing balance	<u>810,900</u>	<u>1,153,220</u>	<u>648,063</u>	<u>—</u>	<u>175,905</u>	<u>2,788,088</u>

Reasons for the changes:

- According to the newly promulgated Company Law and Document Cai Qi [2006] No.67 issued by the Ministry of Finance, an enterprise's balance in statutory public welfare fund as at 31 December 2005 shall be transferred to surplus reserve for its management purposes. The Group transferred its balance in statutory public welfare fund of RMB 179,049,000 to statutory surplus reserve at the end of the Year.
- The liquidation of The Chinese Herbal Medicine Wholesale Division under Guangzhou Chinese Medicine Corporation ("Chinese Medicine Corporation"), a subsidiary of the Company, was completed during the Year, whose surplus reserve amounting to RMB 1,887,000 was transferred to the retained earnings, including statutory surplus reserve of RMB860,000, statutory public welfare fund of RMB413,000 and discretionary surplus reserve of RMB614,000.

### 2. Extracted from the accounts prepared in accordance with HKFRS

Items	Share capital (RMB'000)	Share premium (RMB'000)	Capital reserve (RMB'000)	Statutory surplus reserve (RMB'000)	Statutory public welfare fund (RMB'000)	Discretionary surplus reserve (RMB'000)	Retained earnings (RMB'000)	Total (RMB'000)
As at 1 January 2006	810,900	781,134	421,617	253,130	184,686	129,581	142,075	2,723,123
Profit for the Year	—	—	—	—	—	—	218,067	218,067
Dividend relating to 2005	—	—	—	—	—	—	(56,763)	(56,763)
Transfers	—	—	2,690	230,098	(184,686)	35,408	(83,510)	—
Revaluation of investment properties	—	—	13,116	—	—	—	—	13,116
Disposal of a subsidiary	—	—	—	(154)	—	—	—	(154)
As at 31 December 2006	<u>810,900</u>	<u>781,134</u>	<u>437,423</u>	<u>483,074</u>	<u>—</u>	<u>164,989</u>	<u>219,869</u>	<u>2,897,389</u>



# Changes in Share Capital and Shareholders

## I. CHANGES IN SHARE CAPITAL

### 1. Movement in share capital and its components

	Before change		Change (+/-)					After change	
	Number of shares (share)	Percentage (%)	New issues	Bonus issues (share)	Reserves capitalized	Others	Sub-total (share)	Number of shares (share)	Percentage (%)
I. Shares subject to selling restrictions									
1. State-owned shares	513,000,000	63.26	—	(23,400,000)	—	—	(23,400,000)	489,600,000	60.38
2. Shares held by State-owned legal entities	—	—	—	—	—	—	—	—	—
3. Other domestic shares									
Including: Shares held by									
domestic legal entities	—	—	—	—	—	—	—	—	—
Shares held by									
domestic natural persons	—	—	—	—	—	—	—	—	—
4. Shares held by foreign capital	—	—	—	—	—	—	—	—	—
Including: Shares held by									
overseas legal entities	—	—	—	—	—	—	—	—	—
Shares held by									
overseas natural persons	—	—	—	—	—	—	—	—	—
<b>Total shares subject to selling restrictions</b>	<b>513,000,000</b>	<b>63.26</b>	<b>—</b>	<b>(23,400,000)</b>	<b>—</b>	<b>—</b>	<b>(23,400,000)</b>	<b>489,600,000</b>	<b>60.38</b>
II. Shares not subject to selling restrictions									
1. Renminbi-denominated ordinary shares	78,000,000	9.62	—	23,400,000	—	—	23,400,000	101,400,000	12.50
2. Domestically listed foreign capital shares	—	—	—	—	—	—	—	—	—
3. Overseas listed foreign capital shares	219,900,000	27.12	—	—	—	—	—	219,900,000	27.12
4. Others	—	—	—	—	—	—	—	—	—
<b>Total shares not subject to selling restrictions</b>	<b>297,900,000</b>	<b>36.74</b>	<b>—</b>	<b>23,400,000</b>	<b>—</b>	<b>—</b>	<b>23,400,000</b>	<b>321,300,000</b>	<b>39.62</b>
III. Total shares	<b>810,900,000</b>	<b>100</b>	<b>—</b>	<b>—</b>	<b>—</b>	<b>—</b>	<b>—</b>	<b>810,900,000</b>	<b>100</b>

On 12 April 2006, the Relevant A Shareholders' Meeting of the Company approved the Share Reform Plan of the Company, pursuant to which the holders of circulating A shares were offered 3 shares for every 10 A shares held.

### 2. Issuance and listing of shares

The Company issued 219,900,000 H shares in Hong Kong in October 1997. In January 2001, the Company issued 78,000,000 A shares in the PRC. As at 31 December 2006, the total number of shares issued by the Company amounted to 810,900,000 shares, out of which 60.38% were State-owned shares, approximately 12.50% were A shares and the approximately 27.12% were H shares.

### 3. The inner staff shares

The Company does not have any inner staff shares.





# Changes in Share Capital and Shareholders

## II. INTRODUCTION OF SHAREHOLDERS

### 1. Number of shareholders as at the end of the Reporting Period

As at 31 December 2006, there were 29,932 shareholders in total, out of which 2 shareholders holding the State-owned shares, 29,902 shareholders holding the A shares and the remaining 28 shareholders holding the H shares.

### 2. Shareholders' interests and short positions in the shares and underlying shares of the Company

As at 31 December 2006, the interests and short positions held by the persons (not being the Directors, Supervisors and Senior Management of the Company) in the shares and underlying shares of the Company which were notified to the Company and The Stock Exchange of Hong Kong Limited (the "HKEx") pursuant to Divisions 2 and 3 of Part XV of the Securities and Futures Ordinance (Chapter 571 of the laws of Hong Kong) (the "SFO") and as recorded in the register required to be maintained by the Company under Section 336 of the SFO were as follows:

Shareholders	Nature of shares held	Number of shares held (share)	% of total issued State-owned Shares (%)	% of total issued H shares (%)
Guangzhou Pharmaceutical Holdings Limited ("GPHL")	State-owned shares	468,603,509	Approximately 95.71	—
China Greatwall Asset Management Corporation ("Greatwall Corporation")	State-owned shares	20,996,491	Approximately 4.29	—
The Hongkong and Shanghai Banking Corporation Limited (Note 1)	H shares	61,604,000	—	Approximately 28.01
Standard Chartered Bank (Hong Kong) Ltd. (Note 1)	H shares	54,434,000	—	Approximately 24.75
Greenwoods Asset Management Limited Morgan Stanley Dean Witter	H shares	24,828,000	—	Approximately 11.29
Hong Kong Securities Ltd (Note 1)	H shares	14,171,000	—	Approximately 6.44
Wellington Management Company, LLP	H shares	12,356,000	—	Approximately 5.62
Value Partners Limited (Note 2)	H shares	11,142,000	—	Approximately 5.07
Cheah Cheng Hye (Note 2)	H shares	11,142,000	—	Approximately 5.07

Notes: 1. As notified by HKSCC Nominees Limited, as at 31 December 2006, the H shares held by each corporation in its securities account with the Central Clearing and Settlement System amounted to more than 5% of the total issued H shares of the Company.

2. According to the corporate substantial shareholder notice from Value Partners Limited, 11,142,000 H shares were held by it in its capacity as an investment manager.

According to the individual substantial shareholder notice from Mr. Cheah Cheng Hye, 11,142,000 H shares were held by him by virtue of his interests in Value Partners Limited.

As far as the Directors are aware, as at 31 December 2006, other than those listed above, there was no other person or corporation having an interest or short position in the shares and underlying shares of the Company representing 5% or more of any class of the issued share capital of the Company.



# Changes in Share Capital and Shareholders

## II. INTRODUCTION OF SHAREHOLDERS *(continued)*

### 3. The top ten shareholders of the Company

The top ten shareholders of the Company as at 31 December 2006 are set out as follows:

Shareholders	Nature of shares	No. of shares held (share)	Number of shares subject to selling restrictions (share)	% of total issued share capital (%)	Number of pledged or locked shares (share)
GPHL	State-owned shares	468,603,509	468,603,509	Approximately 57.79	Note (1)
HKSCC Nominees Limited	H shares	218,760,299	—	Approximately 26.98	Unknown
Greatwall Corporation	State-owned shares	20,996,491	20,996,491	Approximately 2.59	Unknown
Bank of China-E Fund Steady Growth Securities Investment Fund	A shares	8,323,466	—	Approximately 1.03	Unknown
Bank of Communications-Ke Hui Securities Investment Fund	A shares	5,038,021	—	Approximately 0.62	Unknown
Western Securities Co., Limited	A shares	4,265,538	—	Approximately 0.53	Unknown
ICBC-Kai Yuan Securities Investment Fund	A shares	3,871,582	—	Approximately 0.48	Unknown
Bank of China-E Fund Strategic Growth No. 2 Mixed Securities Investment Fund	A shares	1,399,801	—	Approximately 0.17	Unknown
ICBC-E Fund Value Selective Stock Securities Investment Fund	A shares	1,199,936	—	Approximately 0.15	Unknown
National Social Security Fund 109 Group	A shares	1,034,508	—	Approximately 0.13	Unknown

Notes:

- (1) During the Reporting Period, the controlling shareholder of the Company, namely GPHL, applied part of its shares of the Company for debt restructure of Guangzhou Baiyunshan Pharmaceutical Co., Ltd. ("Baiyunshan Co., Ltd"). The total number of shares involved was 115,440,000 shares, among which 12,480,000 shares were intended to be transferred to Baiyunshan Co., Ltd. There were still 102,960,000 shares being pledged (including 65,110,000 shares that continued to be frozen on 15 May 2006) as at 31 December 2006.
- (2) According to the information provided by HKSCC Nominees Limited, the H shares held by it were held on behalf of several clients.
- (3) Among the top ten shareholders of the Company, GPHL was not connected with the other nine shareholders and were not persons acting in concert as stipulated in the "Rules Governing the Disclosure of Change in Shareholders' Shareholding in Listed Companies". The Company was not aware of any connection among the other nine shareholders, or whether they were persons acting in concert as stipulated in the "Rules Governing the Disclosure of Change in Shareholders' Shareholding in Listed Companies".



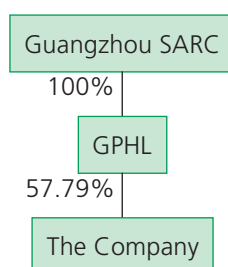
# Changes in Share Capital and Shareholders

## II. INTRODUCTION OF SHAREHOLDERS *(continued)*

### 4. Information of the corporate shareholder holding 10% or more of the Company's total issued shares

<b>Name of shareholder</b>	Guangzhou Pharmaceutical Holdings Limited
<b>% of shares held</b>	57.79%
<b>Legal representative</b>	Yang Rongming
<b>Date of establishment</b>	7 August 1996
<b>Registered capital</b>	RMB1,007.7 million
<b>Business scope</b>	To invest in and manage State-owned assets, to sell and manufacture chemical medicine, Chinese and western medicine, Chinese raw medicine, bio-tech products, medical apparatus, packing materials for pharmaceutical products, health drinks and food, hygienic materials and pharmaceutical related merchandise; to undertake medicine related import and export affairs and to develop real estate.

As at the end of the Reporting Period, the controlling shareholder of the Company was GPL, the beneficial owner of which was the State-owned Assets Regulatory Commission of Guangzhou ("Guangzhou SARC").



### 5. Other shareholders holding 10% or more of the Company's total issued shares

As at the end of the Reporting Period, the Company had no other shareholders holding 10% or more of the Company's total issued shares.

### 6. As at 31 December 2006, the Company's top ten shareholders holding the shares not subject to selling restrictions and their shareholdings were as follows:

Shareholders	No. of shares not subject to selling restrictions held (share)	Nature of shares
HKSCC Nominees Limited	218,760,299	H shares
Bank of China-E Fund Steady Growth Securities Investment Fund	8,323,466	A shares
Bank of Communications-Ke Hui Securities Investment Fund	5,038,021	A shares
Western Securities Co., Limited	4,265,538	A shares
ICBC-Kai Yuan Securities Investment Fund	3,871,582	A shares
Bank of China-E Fund Strategic Growth No. 2 Mixed Securities Investment Fund	1,399,801	A shares
ICBC-E Fund Value Selective Stock Securities Investment Fund	1,199,936	A shares
National Social Security Fund 109 Group	1,034,508	A shares
HSBC Nomiees (Hong Kong) Limited	866,000	H shares
Zhou Zhiping	833,115	A shares

Note: (1) According to the information provided by HKSCC Nominees Limited, the H shares held by it were held on behalf of several clients.

(2) The Company was not aware of any connection among the above-mentioned ten shareholders holding the shares not subject to selling restrictions, or whether they are persons acting in concert as stipulated in the "Rules Governing the Disclosure of Change in Shareholders' Shareholding in Listed Companies".



# Changes in Share Capital and Shareholders

## II. INTRODUCTION OF SHAREHOLDERS *(continued)*

### 7. The top ten shareholders holding shares subject to selling restrictions of the Company as at the end of the Reporting Period

No.	Name of holders of shares subject to selling restrictions	Number of shares subject to selling restrictions held (share)	Listing and trading of shares subject to selling restrictions		Undertakings
			Listing and trading date	Number of additional tradable shares (share)	
1	GPHL	468,603,509	24 April 2007	40,545,000	Note (1)
		428,058,509	24 April 2008	40,545,000	
		387,513,509	24 April 2009	387,513,509	
2	Greatwall Corporation	20,996,491	24 April 2007	20,996,491	Note (2)

Note (1) *The shares subject to selling restrictions held by GPHL shall not be listed and traded, nor transferred within 12 months from the date of implementation of the reform plan. Upon the expiry of such 12 months period, GPHL will not dispose of its shares (which are originally shares subject to selling restrictions) which exceeds 5% and 10% of the total number of the issued shares of the Company in The Shanghai Stock Exchange in the following 12 months and 24 months respectively.*

(2) *The shares held by Greatwall Corporation shall not be within 12 months from the implementation of the Share Reform Plan.*

### 8. Neither the Company nor any of its subsidiaries purchased, sold or redeemed any of the Company's shares during the Reporting Period.

### 9. During the Reporting Period, there was no change in the controlling shareholder of the Company.

## III PUBLIC FLOAT

Based on the publicly available information and to the best knowledge of the Directors, the Company has maintained sufficient public float as at the latest practicable date prior to the date of this report.

## IV PRE-EMPTIVE RIGHTS

According to the Articles of Association of the Company and the laws of the PRC, there is no pre-emptive right, which would oblige the Company to issue new shares to existing shareholders on a pro-rata basis.



# Directors, Supervisors, Senior Management and Staff

## I. PROFILES OF DIRECTORS, SUPERVISORS AND SENIOR MANAGEMENT

### Directors

**Mr. Yang Rongming**, aged 53, Chairman of the Company, is a postgraduate and currently the Chairman and General Manager of GPL. Mr. Yang started his career in October 1970 and served as vice factory manager of Guangzhou Monosodium Glutamate and Food Factory, Deputy General Manager of Guangzhou Ao Sang Monosodium Glutamate & Food Co., Ltd, Director and General Manager of Guangzhou Eagle Coin Enterprises Group Corporation, Chairman and General Manager of Guangzhou Zhujiang Brewery Group Co., Ltd and Chairman of Guangzhou Zhujiang Brewery Co., Ltd. Mr. Yang is also Director of Guangzhou Xing Qun Pharmaceutical Co., Ltd. ("Xing Qun Pharmaceutical"), Guangzhou Zhong Yi Pharmaceutical Co., Ltd. ("Zhong Yi Pharmaceutical") and Guangzhou Pharmaceuticals Corporation ("Pharmaceuticals Corporation") and Chairman of Guangzhou Pharmaceutical Soccer Club Co., Ltd ("GPSC"). Mr. Yang has extensive experience in business management and sales and marketing.

**Mr. Feng Zansheng**, aged 56, Director of the Company, joined GPL in 1970. He graduated from Guangzhou Medical College in 1977 with a Diploma in Medical Treatment. Mr. Feng is the Chairman and General Manager of Pharmaceuticals Corporation, and Vice Chairman of the Chinese Medical Commerce Association. He is also an executive member of Guangdong Medical Society and Vice Commissioner of Trading Specialty. Mr. Feng has extensive experience in corporate management and pharmaceutical trading

**Mr. Chen Zhinong**, aged 46, has been appointed as a Director of the Company since 15 June 2006. Having graduated from a university, he is currently the General Manager of Guangzhou International Group Co. Ltd.. Mr. Chen started his career since November 1983 and served as deputy factory manager and factory manager of Guangzhou Baiyunshan Pharmaceutical General Factory, general manager and chairman of Guangzhou Baiyunshan Enterprise Group Company, Director and Deputy General Manager of GPL, Chairman and General Manager of Guangzhou Han Fang Contemporary Chinese Medicine Research and Development Co., Ltd. ("Guangzhou Han Fang"), and Deputy Chairman of GPSC. Mr. Chen has extensive experience in corporate management and technology research and development.

### Independent Non-executive Directors

**Mr. Wu Zhang**, aged 49, has been an Independent Non-executive Director of the Company since 2000. Mr. Wu is currently an independent director of Guangzhou Zhujiang Industrial Co., Ltd. Mr. Wu received a Master degree in Business Administration from Murdoch University in Australia and has a strong theoretical knowledge in economics and finance and sound experience in securities management. He served as the General Manager of Guangzhou Yue Yin Finance Development Company, Deputy Managing Director of Hong Kong Yue Xiu Finance Co., Ltd and Hong Kong Yue Xiu Securities Co., Ltd., Chairman of Guangzhou Securities Co., Ltd. and Chairman of Golden Eagle Asset Management Co., Ltd.

**Mr. Wong Hin Wing**, aged 44, has been an Independent Non-executive Director of the Company since 26 March 2004. Mr. Wong holds a Master's degree in Executive Business Administration from the Chinese University of Hong Kong. He is a fellow member of the Hong Kong Institute of Certified Public Accountants, the Hong Kong Institute of Directors, the Association of Chartered Certified Accountants, as well as a member of the American Institute of Certified Public Accountants. He is also a fellow member of the Institute of Chartered Secretaries and Administrators and a member of the Securities Institute in the United Kingdom. Mr. Wong is currently the managing director and Responsible Officer of Legend Capital Partners Inc., a licensed corporation under the Securities and Futures Ordinance. He has over 23 years of experience in accounting, finance, investment management and advisory. Mr. Wong had worked with an international audit firm for four years and was the chief financial officer of a listed public company for seven years. He is also a director of Aeon Credit Service (Asia) Company Limited.

**Mr. Zhang Heyong**, aged 67, has been an Independent Non-executive Director of the Company since 26 March 2004. Mr. Zhang graduated from the Medical Science Department of Shanghai Medical University, and is currently the consultant of the State Foods and Medicine Supervisory and Administration, Counselor of State Council, Chairman of the China OTC Medicine Association, Chairman of the Association of China Medicine Quality Control, Chairman of the Association of China Medicine Packaging and Chairman of the Association of China Medicine Packaging Equipment Industry. Mr. Zhang has extensive experience in the pharmaceutical industry.



# Directors, Supervisors, Senior Management and Staff

## I. PROFILES OF DIRECTORS, SUPERVISORS AND SENIOR MANAGEMENT *(continued)*

### Supervisors

**Mr. Chen Canying**, aged 57, Chairman of the Supervisory Committee of the Company, joined GPLH in 1973. Mr. Chen graduated from Guangzhou Administration College in 1985. He served as a Director of Guangzhou Huan Ye Pharmaceutical Co., Ltd ("Guangzhou Huan Ye"). He is also Chairman of the Labor Unions of GPLH and the Company, and the Chairman of Guangzhou Seahorse Advertising Co., Ltd. Mr. Chen is also an executive member of the Guangzhou Entrepreneurs Association, a member of the Editorial Committee of the "Chinese Medicine Affairs Paper", and an executive member of the Chinese Medicine Economic Research Association.

**Mr. Ouyang Qiang**, aged 45, an intermediate economist, has been a Supervisor of the Company since 26 March 2004. Mr. Ouyang graduated from Guangzhou Administration College and was awarded a diploma by the Economics Management University in 2000. He joined GPLH in 1999 and served as the deputy head and the head of the Administration Department of GPLH and the senior manager of the Human Resources Department of the Company. He is currently the factory manager of Guangzhou Chen Li Ji Pharmaceutical Factory ("Chen Li Ji").

**Mr. Zhong Yugan**, aged 50, has been a Supervisor of the Company since 26 March 2004. Mr. Zhong graduated from the Business Economics Department of Beijing Business College in 1982 and was awarded a Bachelor of Arts in economics. He studied abroad in the University of 契里爾•麥托蒂 in the former Yugoslavia from 1985 to 1987. Mr. Zhong is currently the Head of the Business Administration Faculty and a professor in the Guangdong Business College, the professor of management studies and the tutor of Master degree postgraduates. He is also the Vice Chairman of the Association of Marketing Research of China Higher Institutes, committee member of academic work of the Association of China International Public Relations, the Vice Chairman of the Guangdong Provincial Business Economics Association and the Vice Chairman of Guangdong Marketing Association. Mr. Zhong has extensive experience in the fields of marketing and sales, strategic decision-making and corporate management.

### Senior Management

**Mr. Shi Shaobin**, aged 39, has been the General Manager of the Company since 15 June 2006. Mr. Shi received postgraduate education, holds a master degree in Business Administration and is a senior pharmaceutical engineer. After his graduation from the Faculty of Biology and Chemistry of the Zhongshan University in 1989, Mr. Shi served as section member of a research institute, staffer of the sales department, head of the administrative department, assistant to the general manager and manager of the marketing department, and deputy general manager of Guangzhou Jing Xiu Tang Pharmaceutical Co., Ltd. ("Jing Xiu Tang"). In 2001, he obtained a master degree in Business Administration. Mr. Shi served as chairman and general manager of Guangzhou Yangcheng Pharmaceutical Co., Ltd. from 2001 to 2004. Since 2005, he has been a director and chief executive of Guangzhou Wang Lao Ji Pharmaceutical Co., Ltd. ("Wang Lao Ji"). Mr. Shi has extensive experience in production, marketing and operation management.

**Mr. He Shuhua**, aged 50, Deputy General Manager and Company Secretary of the Company, joined GPLH in 1982. He graduated from Zhong Shan University in 1982 with a Bachelor degree in Biology. In 1995, he obtained a master degree in Statistics from the same university. He is also Chairman of Guangxi Ying Kang Pharmaceutical Co., Ltd. ("Guangxi Ying Kang"), Director of Guangzhou Han Fang and China Pharmaceutical Group Co., Ltd, an executive member of Guangdong Statistics Society. Mr. He has been the Company Secretary of the Company since 1997, Deputy General Manager of the Company since September 2001, and served as the Director of the Company from 1 November 2004 to 27 April 2005. He has extensive experience in business management and sales and marketing.

**Mr. Su Guangfeng**, aged 43, Deputy General Manager of the Company since June 2005, with a bachelor degree in industrial studies, joined Baiyunshan Co., Ltd in 1987 and served as the Deputy Chief of the Operation Department of Baiyunshan Co., Ltd and Deputy Plant Head of Guangzhou Baiyunshan Chinese Medicine Factory. He has been the Chairman and General Manager of Xing Qun Pharmaceutical since January 2005. He is also a manager of Ying Bang Branch Company of Guangzhou Pharmaceutical Company Limited ("Ying Bang Company"). Mr. Su has extensive experience in enterprise management, sales and marketing.



# Directors, Supervisors, Senior Management and Staff

## I. PROFILES OF DIRECTORS, SUPERVISORS AND SENIOR MANAGEMENT *(continued)*

### Senior Management *(continued)*

**Mr. Chen Binghua**, aged 41, an accountant with a master degree in Administration, is the Financial Controller and Senior Manager of the Finance Department of the Company. Mr. Chen was General Manager of Shanghai Pudong Xidi Co., Ltd (上海浦东希迪有限公司), General Finance Manager of China Foreign Trade Development Company and Financial Chief of O-NET Communications Ltd. He is also a Director of Guangzhou Bai Di Bio-technology Co., Ltd. ("Guangzhou Bai Di"), Director and Financial Controller of Guangxi Ying Kang and Supervisor of China Pharmaceutical Group Co., Ltd. He has been the Senior Manager of the Finance Department of the Company since 2002 and the Financial Controller of the Company since December 2005. Mr. Chen has extensive experience in accounting and financial management.

## II. DIRECTORS', SUPERVISORS' AND SENIOR MANAGEMENT'S INTERESTS IN SHARES (A SHARES) OF THE COMPANY DURING THE REPORTING PERIOD

Name	Position	Shares held as at the beginning of the Reporting Period (share)	Shares held as at the end of the Reporting Period (share)	Reason for change
Yang Rongming	Chairman	—	—	—
Chen Zhinong	Executive Director (appointed on 15 June 2006)	—	—	—
Feng Zansheng	Executive Director	—	—	—
Wu Zhang	Independent Non-executive Director	—	—	—
Wong Hin Wing	Independent Non-executive Director	—	—	—
Zhang Heyong	Independent Non-executive Director	—	—	—
Zhou Yuejin	Vice Chairman (resigned on 27 April 2006)	28,900	37,570	Bonus shares as a result of the Share Reform Plan
Xie Bin	Executive Director and General Manager (resigned on 15 June 2006)	1,000	1,300	Bonus shares as a result of the Share Reform Plan
Chen Canying	Chairman of the Supervisory Committee	9,800	12,740	Bonus shares as a result of the Share Reform Plan
Ouyang Qiang	Supervisor	10,100	13,130	Bonus shares as a result of the Share Reform Plan
Zhong Yugan	Supervisor	—	—	—
Shi Shaobin	General Manager (appointed on 15 June 2006)	—	—	—
He Shuhua	Deputy General Manager and Company Secretary	27,700	36,010	Bonus shares as a result of the Share Reform Plan
Su Guangfeng	Deputy General Manager	—	—	—
Chen Binghua	Financial Controller	4,800	6,240	Bonus shares as a result of the Share Reform Plan





# Directors, Supervisors, Senior Management and Staff

## III. DIRECTORS', SUPERVISORS' AND SENIOR MANAGEMENT'S INTERESTS AND SHORT POSITIONS IN THE SHARES, UNDERLYING SHARES AND DEBENTURES OF THE COMPANY

1. As at 31 December 2006, the interests or short positions of the Directors, Supervisors and Senior Management in the shares, underlying shares and debentures of the Company or any of its associated corporations (within the meaning of Part XV of the SFO), which were notified to the Company and the HKEx pursuant to Divisions 7 and 8 of Part XV of the SFO (including interests or short positions which they are taken or deemed to have under such provisions of the SFO), or which were required, pursuant to Section 352 of the SFO, to be recorded in the register referred therein, or which were required pursuant to the Model Code for Securities Transactions by Directors of Listed Companies ("Model Code") of the Rules Governing the Listing of Securities on HKEx (the "Listing Rules") to be notified to the Company and the HKEx were as follows:

### Directors

Name	Type of interest	Company	Number of shares
Zhou Yuejin	Personal	A shares of the Company	37,570
Xie Bin	Personal	A shares of the Company	1,300
Feng Zansheng	Personal	Pharmaceuticals Corporation	700,000

### Supervisors

Name	Type of interest	Company	Number of shares
Chen Canying	Personal	A shares of the company	12,740
Ouyang Qiang	Personal	A shares of the company	13,130

### Senior Management

Name	Type of interest	Company	Number of shares
Shi Shaobin	Personal	Jing Xiu Tang	25,000
He Shuhua	Personal	A shares of the company	36,010
Chen Binghua	Personal	A shares of the company	6,240

2. Save as disclosed above, as at 31 December 2006, none of the Directors, Supervisors, Senior Management and their associates had any personal, family, corporate or other interests or short positions in the shares, underlying shares or debentures of the Company or any of its associated corporation (within the meaning of Part XV of the SFO) which would have to be notified to the Company and the HKEx pursuant to Divisions 7 and 8 of Part XV of the SFO (including interests or short positions which they are taken or deemed to have under such provisions of the SFO), or which were required, pursuant to Section 352 of the SFO, to be entered in the register referred therein, or which were required, pursuant to the Model Code of the Listing Rules, to be notified to the Company and the HKEx.



# Directors, Supervisors, Senior Management and Staff

## IV. EMOLUMENTS FOR THE YEAR

### 1. Policy on determining emoluments

The annual emoluments for Directors and Supervisors were proposed by the Board and approved at the Annual General Meeting of the Company at which the Board was authorized to determine the amount of emoluments and method of payment for services of the Company's Directors and Supervisors. The amount of emoluments and payment method for the Senior Management were determined by the Board after taking into account of the Company's operating results and individual performance.

### 2. Emoluments for the Year

During the Year, the total emoluments of the Directors, Supervisors and Senior Management of the Company who received emoluments from the Group amounted to RMB3,217,000, details of which are set out as follows:

Name	Emoluments received from the Group		Whether received emoluments from the Company's shareholder or connected parties
	Whether received emoluments from the Group	Total emoluments for the Year (RMB' 000)	
<b>Directors</b>			
Yang Rongming	No	—	Yes
Feng Zansheng	Yes	611	No
Chen Zhinong	No	—	Yes
Wu Zhang	Yes	80	No
Wong Hin Wing	Yes	80	No
Zhang Heyong	Yes	80	No
Zhou Yuejin	Yes	232	No
Xie Bin	Yes	377	No
<b>Supervisors</b>			
Chen Canying	No	—	Yes
Ouyang Qiang	Yes	157	No
Zhong Yugan	Yes	30	No
<b>Senior Management</b>			
Shi Shaobin	Yes	622	No
He Shuhua	Yes	299	No
Su Guangfeng	Yes	454	No
Chen Binghua	Yes	195	No



# Directors, Supervisors, Senior Management and Staff

## IV. EMOLUMENTS FOR THE YEAR *(continued)*

### 2. Emoluments for the Year *(continued)*

- Notes: (1) Mr. Zhou Yuejin resigned on 27 April 2006. His emoluments for the Year were the emoluments received from the Company as taking his original duties for the period from 1 January 2006 to the date of his resignation;
- (2) Mr. Xie Bin resigned on 15 June 2006. His emoluments for the Year were the emoluments received from the Company as taking his original duties for the period from 1 January 2006 to the date of his resignation;
- (3) Mr. Shi Shaobin was appointed on 15 June 2006. His emoluments for the Year were the emoluments received from a subordinated company of the Company as taking his original duties for the Year;
- (4) Mr. Ouyang Qiang has been the factory manager of Chen Li Ji, a subsidiary of the Company, since July 2006. His emoluments for the Year include the emoluments received from the subsidiary from July to December of the Year;
- (5) The emoluments of Mr. Feng Zansheng and Mr. Su Guangfeng for the Year were the emoluments they received from the Company's subsidiaries as taking their duties, and the emoluments of Mr. Wu Zhang, Mr. Wong Hin Wing, Mr. Zhang Heyong, Mr. Zhong Yugan, Mr. He Shuhua and Mr. Chen Binghua were the emoluments they received from the Company for the Year.
- (6) Details of the emoluments of the Directors, Supervisors and Senior Management for the Year are set out on the notes to the accounts on pages 180 to 182.

## V. APPOINTMENT AND RESIGNATION OF DIRECTORS, SUPERVISORS AND SENIOR MANAGEMENT DURING THE REPORTING PERIOD

- 1 As approved at the 22nd meeting of the Third Session of the Board, Mr. Zhou Yuejin resigned as the Director and Vice Chairman of the Company.
- 2 At the Company's Annual General Meeting of 2005, Mr. Chen Zhinong was elected as the Executive Director of the Third Session of the Board of the Company, with a term of office commencing from the date of his appointment until the date of election of the new session of the Board of the Company.
- 3 As approved at the 23rd meeting of the Third Session of the Board, Mr. Xie Bin resigned as the Director and the General Manager of the Company.
- 4 As approved at the 23rd meeting of the Third Session of the Board, Mr. Shi Shaobin was appointed as the General Manager of the Company, with a term of office commencing from the date of appointment until the date of election of the new session of the Board of the Company.



# Directors, Supervisors, Senior Management and Staff

## VI. DIRECTORS' AND SUPERVISORS' SERVICE CONTRACTS

Each of the present Directors and Supervisors has entered into a service contract with the Company. Details are set out as follows:

<b>Directors</b>	<b>Contract term</b>
Mr.Feng Zansheng (Executive Director), Mr. Wu Zhang, Mr.Wong Hin Wing and Mr.Zhang Heyong (Independent Non-executive Directors)	Commencing from 26 March 2004 up to the date of election of the Fourth Session of the Board
Mr.Yang Rongming (Executive Director)	Commencing from 1 November 2004 up to the date of election of the Fourth Session of the Board
Mr. Chen Zhinong (Executive Director)	Commencing from 15 June 2006 up to the date of election of the Fourth Session of the Board
Mr. Shi Shaobin (Executive Director)	Commencing from 2 April 2007 up to the date of election of the Fourth Session of the Board
<b>Supervisors</b>	<b>Contract term</b>
Mr. Chen Canying, Mr. Ouyang Qiang and Mr. Zhong Yugan	Commencing from 26 March 2004 up to the date of election of the Fourth Session of the Supervisory Committee

The term of office of each Director and Supervisor of the Company commenced from the date of their respective appointments to the date of election of the Fourth Session of the Board and the Fourth Session of the Supervisory Committee. The term of each session of the Board or the Supervisory Committee shall be approximately three years. All Directors and Supervisors are eligible to offer themselves for re-election.

The above-mentioned service contracts with the Directors and Supervisors do not contain any provisions for compensation for early termination of contract, or for failure in being re-elected after expiration of their term of office.

## VII. DIRECTORS' AND SUPERVISORS' INTERESTS IN CONTRACTS

No contract of significance in relation to the business of the Group to which the Company, its subsidiaries or its holding company was a party and in which a Director or Supervisor 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, Supervisors, Senior Management and Staff

## VIII. MODEL CODE FOR SECURITIES TRANSACTIONS BY DIRECTORS AND SUPERVISORS

During the Reporting Period, the Company adopted Appendix 10 of the Listing Rules titled “Model Code for Securities Transactions by Directors of Listed Issuers” as the code for securities transactions by Directors and Supervisors of the Company. After making specific inquiry of all the Directors and Supervisors, the Company confirmed that its Directors and Supervisors had fully complied with the standard laid down in the said rules.

## IX. EMPLOYEES OF THE GROUP

As at 31 December 2006, the number of employees on the payroll register of the Group was 8,223, including:

	<b>No. of employees</b>
Production and supporting staff	3,639
Sales personnel	2,335
Technical, research and engineering staff	1,066
Finance and statistics staff	308
Other administrative staff	875

100 of the employees were holders of a master degree and 1,291 were holders of a bachelor degree. The number of retirees was 4,967. The total salary payment for the Year was approximately RMB418 million.

The remuneration of the employees of the Group included salaries, bonuses and other fringe benefits. The Group, in compliance with the relevant PRC rules and regulations, applied different rates of remuneration to different employees, based on the employees' performance, experience, position and other factors.



# Corporate Governance

## I. CORPORATE GOVERNANCE

During the Reporting Period, the Company has been operating in strict compliance with the PRC Company Law (the "Company Law"), the Securities Law, the listing rules of The Shanghai Stock Exchange and HKEx and other requirements set out in the relevant rules and regulations issued by the CSRC, devoting to improving its corporate governance structure and regulating its operation. In accordance with the spirit of the Notice on Urging Listed Companies to Amend the Articles of Association (Zheng Jian Gong Si Zi [2005] No.15), the Company, based on its actual conditions, amended such documents as the Articles of Association, Rules and Procedures for Shareholders' General Meetings and Rules and Procedures for Board Meetings with reference to the Code of Corporate Governance for Listed Companies, Regulations on Reinforcement of Protection of Interests of Public Shareholders, the revised listing rules of the Shanghai Stock Exchange and HKEx and other relevant laws and regulations, so as to regulate its operations, improve our current corporate system and protect the interest of the medium and minority shareholders.

### 1. Shareholders and general meeting of shareholders

The Company is endeavored to ensuring equality among all shareholders, especially the minority shareholders so that they can fully exercise their rights and undertake their obligations accordingly, and to ensure that the shareholders will be informed and are able to participate in the important matters of the Company specified in laws, administrative regulations and the Articles of Association, establishing an effective channel for the Company to communicate with the shareholders.

The general meeting of shareholders is the highest authority of the Company and it exercises its power in accordance with the laws. It decides the important matters of the Company. The annual general meeting of shareholders or the extraordinary general meetings of shareholders provide a channel for the management to communicate directly with the shareholders. The general meeting of shareholders is convened and held in strict compliance with the Standard Opinions on Shareholders' General Meetings issued by CSRC and Rules and Procedures for Shareholders' General Meetings of the Company. The Company complies strictly with the relevant requirements in respect of voting matters and voting procedures so as to safeguard the legal interests of the Company and its shareholders. The accountant and the lawyer will present at the meeting as witnesses. The Company encourages all shareholders to attend the meetings and welcome shareholders to express their opinions at the meetings.

### 2. Relationship between the controlling shareholder and the Company

GPHL, as the controlling shareholder of the Company, exercises its power and accepts its obligations in accordance with the laws, and has not acted beyond the shareholders' meetings to interfere directly or indirectly in the Company's operations. The Company and GPHL have been working separately in respect of assets, business, organization, finance and human resources and are independent of each other. The Board, the Supervisory Committee and the internal organizations of the Company can operate independently.

### 3. Board of Directors

#### (1) Composition

The Board is the core decision-making body entrusted by general meeting of the shareholders to be in charge of the operation and management of the Company's assets. The Board is accountable to the Shareholders.

The present Board is the third session since the establishment of the Company. It consists of 7 members, of which there are 4 Executive Directors and 3 Independent Non-executive Directors. Each Director has a term of office commencing from 26 March 2004 or the date of their respective appointments to the date of election of a new session of the Board.



## I. CORPORATE GOVERNANCE *(continued)*

### 3. Board of Directors *(continued)*

#### (1) Composition *(continued)*

Directors shall be elected or removed by general meeting of shareholders, at which a cumulative voting system is adopted for the election of directors. Directors are eligible for re-election upon expiration of their term of office. All Independent Non-executive Directors are independent persons, and are not connected with the Company and its substantial shareholders. Their terms of office shall not exceed six years.

The role of Chairman and General Manager of the Company are performed by separate persons with clear division of responsibilities. The Board is presided over by the Chairman, who is in charge of the routines of the Board and the examination of the carrying out of the resolutions passed at Board meetings. The General Manager works under the leadership of the Board. The principal responsibilities of the General Manager include management of the Company's daily operations and implementation of the resolutions passed at the Board.

Members of the Board have different industry backgrounds, having expertise and extensive experience in areas of business management, accounting, finance, pharmaceuticals and investment planning.

#### (2) Board Meetings

During the year, ten Board meetings were held, at which the investment projects, connected transactions and financial matters of the Group were discussed. Effective discussions and prudent decisions were made at such meetings. All the Directors of the Company can obtain from the Company Secretary and the Secretariat to the Board of the Company timely relevant information and updates of the statutory and regulatory regulations that directors of listed companies must be abided by and that are related to their continuing obligations to ensure that the Directors understand their duties and that the procedures of Board meetings are implemented and complied with appropriately. The Directors and the special committees of the Board are both entitled within the scope of their powers to engage the services of independent professional institutions for performing their duties or for the business operation when needed. The Company shall bear the reasonable cost incurred thereof.

The attendance of Directors at Board meetings during the Reporting Period is set out below:

Directors	Required Meetings Attendance	Meetings attended in person <i>(frequencies)</i>	Meetings attended by proxy <i>(frequencies)</i>	Absence <i>(frequencies)</i>	Remarks
Mr. Yang Rongming	10	9	1	/	Appointed Mr. Chen Zhinong to attend and vote on his behalf
Mr. Chen Zhinong (appointed on 15 June 2006)	6	4	2	/	Appointed Mr. Yang Rongming to attend and vote on his behalf
Mr. Feng Zansheng	10	10	/	/	—
Mr. Wu Zhang	10	10	/	/	—
Mr. Wong Hin Wing	10	10	/	/	—
Mr. Zhang Heyong	10	10	/	/	—
Mr. Zhou Yuejin (resigned on 27 April 2006)	3	3	/	/	—
Mr. Xie Bin (resigned on 15 June 2006)	4	4	/	/	—





# Corporate Governance

## I. CORPORATE GOVERNANCE *(continued)*

### 3. Board of Directors *(continued)*

#### (3) The Independent Non-executive Directors

Currently, the Company has 3 Independent Non-executive Directors, representing more than 1/3 of the total members of the Board. All the Independent Non-executive Directors of the Company are familiar with the rights and obligations of directors and independent non-executive directors of listed companies. During the Reporting Period, the Independent Non-executive Directors attended Board meetings and general meetings of shareholders in a careful, responsible and active manner. They had done a lot of work on improving the Company's corporate governance and material decision-making, and had expressed impartial and objective opinions on relevant matters, thus effectively safeguarding the interests of the shareholders. All of the 3 Independent Non-executive Directors of the Company were members of the special committees formed under the Board.

During the Reporting Period, the Independent Non-executive Directors of the Company worked diligently, attended meetings of the Board as scheduled, expressed their independent views on the connected transactions made during the Reporting Period and discharged their duties as Independent Non-executive Directors seriously.

During the Reporting Period, the Independent Non-executive Directors of the Company expressed no dissenting views to the Board resolutions and other matters other than Board resolutions.

The Board confirmed receipt from each of the Independent Non-executive Directors a confirmation letter in regards to his independence pursuant to Rule 3.13 of the Listing Rules of HKEx. The Board considered the existing Independent Non-executive Directors to be independent persons as defined in Rule 3.13 of the Listing Rules of HKEx.

#### (4) Loan or guarantee for loan granted to the Directors

During the Reporting Period, the Group had not made any loan or provided any guarantee for any loan, directly or indirectly, to the Directors, Supervisors and Senior Management of the Company, the Company's controlling shareholder or their respective connected persons.

### 4. Committees of the Board

#### (1) Audit Committee

In August 1999, the Company established an Audit Committee. Its principal responsibilities include: to review and monitor the quality, quantity and procedure of the Group's financial reporting; to review the completeness and effectiveness of the Company's internal control system; to consider the appointment of independent auditors and co-ordinate and to review the efficiency and quality of their work.

The Audit Committee now comprises Mr. Wong Hin Wing (Head of the Committee), Mr. Wu Zhang and Mr. Zhang Heyong. All three of them are Independent Non-executive Directors of the Company and are qualified under relevant requirements. The term of office of the members of the Audit Committee commences from their appointments on 26 March, 2004 to the date of election of the new session of the Board. In 2006, the Audit Committee had held two meetings, which were chaired by Mr. Wong Hin Wing. All of the committee members have attended each meeting.

All the resolutions passed at the Audit Committee meetings were recorded and filed in accordance with the relevant requirements.



## I. CORPORATE GOVERNANCE *(continued)*

### 4. Committees of the Board *(continued)*

#### (1) Audit Committee *(continued)*

The followings were the major work completed by the Audit Committee during the Year:

- Review the annual, interim and quarterly results and financial reports of the Company, and management proposals issued by the external auditors and the reply from our management thereto;
- Review matters related to the accounting policies and accounting practices adopted by the Group; and
- Give advice on the material matters of the Company or remind management of relevant risks.

#### (2) Investment Management Committee

In February 2001, the Company established an Investment Management Committee. Its principal responsibilities are to examine and review the strategic development of the Company, to formulate strategic plans and to control significant capital operations, assets operations and the implementation of investment projects.

The Investment Management Committee now comprises Mr. Yang Rongming (Head of the Committee) and Mr. Feng Zansheng. All of whom are Executive Directors. Mr. Zhou Yuejin and Mr. Xie Bin, the former members of the committee, resigned on 27 April, 2006 and 15 June, 2006 respectively. The term of office of the members of the Investment Management Committee commences from the date of their respective appointments to the date of election of the new session of the Board. During the Reporting Period, the Investment Management Committee held three meetings, at which the investment projects and investment proposals were considered. All of the committee members had attended each meeting.

#### (3) Remuneration & Evaluation Committee

In February 2002, the Company established a Remuneration & Evaluation Committee. Its principal responsibilities are to consider or formulate the remuneration policies and incentive mechanism and their implementation, and to give proposals on the performance assessment, appointment and removal and nominations of Directors and Senior Management.

The Remuneration & Evaluation Committee now comprises of Mr. Yang Rongming, an Executive Director, and three Independent Non-executive Directors, Mr. Wu Zhang (Head of the Committee), Mr. Wong Hin Wing and Mr. Zhang Heyong. The term of office of the aforementioned committee members commences from the date of their respective appointments to the date of election of the new session of the Board.

### 5. The Supervisory Committee

The Supervisory Committee exercised their supervision power legally to safeguard the lawful interests of the shareholders, the Company and employees. The number and composition of the Supervisory Committee of the Company comply with the relevant laws and regulations. During the Reporting Period, three meetings were held by the Supervisory Committee. All members of the Supervisory Committee attended all the meetings to monitor the Company's financial conditions and the legitimacy of performance of the Company's Directors and Senior Management on behalf of the shareholders. They also attended all the meetings of the Board and discharged their duties seriously.



# Corporate Governance

## I. CORPORATE GOVERNANCE *(continued)*

### 6. Other interested parties

The Company respected and safeguarded the interests of the interested parties and realized the balance of interests among the shareholders, employees and the society so as to mutually promote the sustainable and sound development of the Company.

### 7. Information disclosure and management of relationship with investors

The Company delegated the Company Secretary with the responsibility for the Company's information disclosure, handling company visits and enquiries from shareholders and investors, responding to correspondence from shareholders in a timely manner. It designated Shanghai Securities in the Mainland and Hong Kong Economic Times and The Standard in Hong Kong to publish the Company's information. It continued to disclose information in a truthful, accurate, comprehensive and timely manner in strict compliance with the relevant rules and regulations and the Code of Information Disclosure formulated by the Company. The Company also ensures that all shareholders have fair access to information relating to the Company.

## II. SEPARATION OF BUSINESS, HUMAN RESOURCES, ASSETS, ORGANIZATION AND FINANCIAL ARRANGEMENT FROM THE CONTROLLING SHAREHOLDER

- 1. Separation of business:** the Company operates with an extensive business scope that is independent from its controlling shareholder.
- 2. Human resources:** The Company maintains independency in areas of staffing, personnel and payroll management. The General Manager, Deputy General Manager, Company Secretary, Financial Controller, and other senior executives of the Company are remunerated by the Company.
- 3. Assets:** The Group is equipped with an independent production system, a supplementary production system and related facilities. It also has its own independent purchases and sales systems. There are currently 36 trademarks used by the Group, the titles of which are vested with GPL, the controlling shareholder of the Company. The Company has entered into an agreement with GPL in relation to the use of trademarks. In addition, the Company owns 4 trademarks, the registrations of which are still valid.
- 4. Organization:** The Company has its own independent and comprehensive organizational structure. The Board, the Supervisory Committee and other departments are operating independently and autonomously. Further, they possess independent decision-making mechanisms and complete production units. There does not exist any supervisory or reporting relationships with the functional departments of the controlling shareholder of the Company.
- 5. Finance:** The Company has established an independent finance department, has set up an independent accounting system and has formulated an independent financial management policy. The Company has maintained separate bank accounts and paid tax independently.



## III. INTERNAL CONTROLS

The Board is responsible for establishing and maintaining the Company's internal control system, reviewing the effectiveness of all important monitoring procedures relating to finance, operation, compliance and risk management, and the protection of shareholders' interests and the Group's assets. The Board authorizes the Company's management to promote the establishment of internal control system, and the Audit Committee to review effectiveness of such system.

Since the establishment of the Company in 1997, it has been committed to establish and improve its corporate governance, has have set up a comprehensive corporate governance structure and established gradually a series of rules for corporate governance and internal control. Besides, the Company has also built in an operation management system covering aspects like production management, sourcing management, sales and marketing, financial management, investment, R & D, human resources, information system management. For its implementation, specific relevant management requirements are developed.

The Board considers that the Company has built in various internal control systems to mitigate risks. Those systems have been improving to suit the needs during the Company's continuous development process and they cover each level of the Company's structure and every aspect of the Company's business activities and internal management. They are effectively implemented. In short, they are effective as a whole without any significant defect.

However, to fully review the effectiveness of the Company's internal control system and its further fine-tuning, the Company has taken or will take the following actions:

- (1) set up an audit department on 26 October 2006 as the Company's internal auditing department and internal body for monitoring, inspection and supervision;
- (2) named the year 2007 as the "Fundamental Management Year", transferred some of the core staff to establish a committee for fundamental management, actively promote the idea to the subsidiaries, engage professionals to play a part in the activities of the "Fundamental Management Year";
- (3) will amend our "Internal Control System Handbook" specifically prepared for the Company according to the "Corporate Internal Control System-fundamental Rules" of the Ministry of Finance and 26 specific rules, endeavour to perfect the Company's internal control system, evaluate the effectiveness of such system and strengthen the implementation of the internal control system and prevent any corporate risk arising.



## Summary of the Shareholders' Meetings

During the Reporting Period, one annual general meeting and one extraordinary general meeting have been convened, details of which are set out as follows:

<b>Session and number of meeting</b>	<b>Convening date</b>	<b>Newspapers for publication of the resolutions</b>	<b>Disclosure date</b>
First Extraordinary General Meeting of 2006	12 April 2006	Shanghai Securities in the PRC, Hong Kong Economic Times and The Standard in Hong Kong	13 April 2006
2005 Annual General Meeting	15 June 2005		16 June 2006



# Report of the Board of Directors

(Unless otherwise stated, the financial data contained in this report is extracted from the Group's accounts prepared in accordance with the PRC Accounting Standards and Systems)

## MANAGEMENT DISCUSSION AND ANALYSIS

### (i) Business Scope and Analysis of Operations

#### 1. Scope of business

The Group is principally engaged in (1) the manufacture and sales of Chinese Patent Medicine ("CPM"); (2) wholesale, retail, import and export of western and Chinese pharmaceutical products and medical apparatus; and (3) research and development of natural medicine and biological medicine.

#### 2. Analysis of operating results

##### (1) Operation review

The year 2006 marked a start under the 11th Five-Year Plan of the Company, in which the Company faced new opportunities and challenges. During the Year, policies for adjustment of and fixing the prices of medicine were introduced. Anti-corruption measures were implemented in order to curb the bribes, regulating and restoring order in the pharmaceutical market. Coupled with the stricter supervision of the domestic pharmaceutical industry, there were dramatic changes in the operational environment of the domestic pharmaceutical manufacturing industry and the distribution industry.

Amid the adverse factors of increasingly fierce domestic competition in 2006, the Company stuck to the idea of "realization of rapid growth in both sales and scale through technological innovation with marketing innovation". The Group took a series of effective measures to promote innovative technology, explore the market, integrate internal resources, effectively use the capital, and enhance fundamental internal management system, resulting in positive prospects for the Group's operations.

According to PRC Accounting Standards and Systems, the Group recorded turnover of RMB10,241,004,000 for 2006, up 13.46% as compared with 2005. The profit before tax amounted to RMB370,362,000, representing an increase of 20.74% over 2005 and net profit amounted to RMB 227,328,000, representing an increase of 23.23% over 2005. According to HKFRS, the Group recorded turnover of RMB10,241,004,000 for the Year, up 13.46% as compared with 2005. Profit before income tax amounted to RMB349,155,000, representing an increase of 10.67% over 2005 and profit attributable to equity holders of the Company amounted to RMB218,067,000, representing an increase of 10.24% over 2005.



# Report of the Board of Directors

## MANAGEMENT DISCUSSION AND ANALYSIS *(continued)*

### (i) Business Scope and Analysis of Operations *(continued)*

#### 2. Analysis of operating results *(continued)*

##### (1) Operation review *(continued)*

A breakdown of the operational results of the overall and principal operations of the Group for 2006 is set out as follows:

*Prepared in accordance with PRC Accounting Standards and System*

Items	2006 (RMB'000)	2005 (RMB'000)	Growth (YoY)(%)
<b>Turnover</b>	<b>10,241,004</b>	9,026,340	13.46
Include: Manufacturing	<b>2,412,184</b>	2,141,675	12.63
Trading	<b>7,828,820</b>	6,884,665	13.71
<b>Profit before tax</b>	<b>370,362</b>	306,741	20.74
Include: Manufacturing	<b>278,466</b>	231,705	20.18
Trading	<b>91,896</b>	75,036	22.47
<b>Net profit</b>	<b>227,328</b>	184,482	23.23
Include: Manufacturing	<b>177,015</b>	135,534	30.61
Trading	<b>50,313</b>	48,948	2.79

*Prepared in accordance with HKFRS*

<b>Turnover</b>	<b>10,241,004</b>	9,026,340	13.46
Include: Manufacturing	<b>2,412,184</b>	2,141,675	12.63
Trading	<b>7,828,820</b>	6,884,665	13.71
<b>Profit before income tax</b>	<b>349,155</b>	315,493	10.67
Include: Manufacturing	<b>260,772</b>	245,829	6.08
Trading	<b>88,383</b>	69,664	26.87
<b>Profit attributable to equity holders of the Company</b>	<b>218,067</b>	197,804	10.24
Include: Manufacturing	<b>174,538</b>	152,088	14.76
Trading	<b>43,529</b>	45,716	(4.78)





# Report of the Board of Directors

## MANAGEMENT DISCUSSION AND ANALYSIS (continued)

### (i) Business Scope and Analysis of Operations (continued)

#### 2. Analysis of operating results (continued)

##### (1) Operation review (continued)

Analysis of the Group's turnover and profit from principal activities for the Year is set out as follows:

	Turnover		Profit from principal activities	
	Under PRC Accounting Standards and Systems (RMB'000)	Under HKFRS (RMB'000)	Under PRC Accounting Standards and Systems (RMB'000)	Under HKFRS (RMB'000)
Principal activities:				
Manufacturing and sales	2,412,184	2,412,184	1,239,694	1,258,638
Trading				
Including:				
Wholesale	7,267,373	7,267,373	416,290	421,638
Retail	335,872	335,872	71,668	72,689
Import and export	225,575	225,575	15,533	15,811
Sub-total	7,828,820	7,828,820	503,491	510,138
Total	10,241,004	10,241,004	1,743,185	1,768,776

Geographical analysis of sales arising from the manufacturing operations and trading operations of the Group is set out as follows:

Region	Manufacturing		Trading		Consolidated (RMB'000)	Percentage of the total turnover (%)
	Turnover (RMB'000)	Percentage of the manufacturing turnover (%)	Turnover (RMB'000)	Percentage of the trading turnover (%)		
Southern China	1,575,392	65.31	6,700,572	85.59	8,275,964	80.81
Eastern China	322,887	13.39	446,034	5.70	768,921	7.51
Northern China	168,023	6.97	169,556	2.17	337,579	3.30
North-Eastern China	131,533	5.45	86,130	1.10	217,663	2.13
South-Western China	143,645	5.95	249,521	3.19	393,166	3.84
North-Western China	69,294	2.87	72,739	0.93	142,033	1.39
Exports	1,409	0.06	104,269	1.32	105,678	1.02
Total	2,412,183	100.00	7,828,821	100.00	10,241,004	100.00



# Report of the Board of Directors

## MANAGEMENT DISCUSSION AND ANALYSIS *(continued)*

### (i) Business Scope and Analysis of Operations *(continued)*

#### 2. Analysis of operating results *(continued)*

##### (1) Operation review *(continued)*

During the Reporting Period, a number of measures were taken to enhance the Manufacturing Operations of the Group in the following areas: (1) Resources were devoted to promote the image of both the brands and products through various means and channels. It also made earnest efforts to improve the distribution network and to further explore the three major end markets, namely hospitals, retail vendors, and communities and rural markets. During the Year, the Group successfully held product exhibitions and customers' parties in various cities such as Qingdao, Nanjing and Tangshan. In addition, the Group actively launched a football promotion campaign and made good use of the GPL's Annual Technology Innovation and Medicine Safety Forum (廣藥集團年度科技創新暨用藥安全高峰論壇) and the awards of "China Time-honored Brand" (「百年中華老字號」) to its numerous brands, including Wang Lao Ji, Jing Xiu Tang, Pan Gao Shou and Cai Zhi Lin, to enhance the Group's image and reputation as the largest Chinese Patent Medicine producer with many "China Time-honored Brands" and facilitate the development of its core business. (2) The Group strengthened strategic cooperation with major distributors throughout China and through other effective distribution management measures to increase the market prices of products in a steady and gradual manner, striving to explore market for core products such as diabetes curing medicine, cerebrovascular medicine, heat clearing and anti-toxic medicine, cough and phlegm clearing medicine; (3) More resources were allocated by the Group on research and development as well as mass production of new products. During the Year, production approval for Kun Xian Capsule (formerly known as "Feng Shi Ping Capsule") was granted. The initial preparation work for marketing activities is currently in progress. Clinical research on rabies bacterin was completed and application for the production approval is also under way. (4) The internal control was further strengthened down to the base-level. On the financial aspect, better controls over budget, funding and receivables were implemented; on the operations aspect, higher standards were set to minimize operations risks.

In 2006, there were 36 products whose sales income exceeded RMB10 million, of which annual sales income exceeding RMB100 million included Xiao Ke Wan, Hua Tuo Zai Zao Wan, Xia Sang Ju Ke Li and the series of Wang Lao Ji Guangdong Liang Cha, the annual sales income of 4 products ranged from RMB30 million to RMB100 million and the annual sales income of 18 products ranged from RMB10 million to RMB30 million. The sales income for the Year of certain key products such as Wang Lao Ji Qing Liang Cha, Zhui Feng Tou Gu Wan, Mi Lian Chuan Bei Pi Pa Gao, Hua Zhi Shuan, Xia Sang Ju Ke Li, Guangdong Liang Cha Ke Li and Xiao Er Qi Xing Cha increased significantly by 133.20%, 43.21%, 35.98%, 75.66%, 17.64%, 24.14% and 53.72% respectively as compared with the previous year.

During the Reporting Period, sales of heat clearing and anti-toxic medicine, cough and phlegm clearing medicine, diabetes curing medicine and arthritis curing medicine for the Manufacturing Operations increased by 26.41%, 6.08%, 9.22% and 16.49% as compared with the previous year respectively, while sales of gastric medicine decreased by 19.58% as compared with the previous year.



# Report of the Board of Directors

## MANAGEMENT DISCUSSION AND ANALYSIS (continued)

### (i) Business Scope and Analysis of Operations (continued)

#### 2. Analysis of operating results (continued)

##### (1) Operation review (continued)

Analysis of sales of major products for the Manufacturing Operations in 2006 is as follows:

Products	Sales income (RMB'000)	Gross profit (RMB'000)
Heat clearing and anti-toxic	627,938	302,934
Including: herb tea series	180,672	76,381
Diabetes curing	444,000	303,918
Cough and phlegm clearing	269,633	154,243
Arthritis curing	284,232	167,592
Gastric	79,751	37,320
Other products	706,629	292,630

Notes:

(1) Herb tea series includes Wang Lao Ji herb tea and Xing Qun Xia Sang Ju drinks.

(2) In the above chart, the sales of the products of Wang Lao Ji were calculated by the percentage of shareholding in Wang Lao Ji by the Company, namely 48.0465%.

During the Year, the Group continued to accelerate the construction of technology platforms and to strengthen the research and development of new products. In 2006, products such as Kun Xian Capsule and Nateglinide Tablet obtained production approvals on new medicine and three products obtained the approvals on clinical research.

During the Reporting Period, the Group took the following measures in the Trading Operations of the Group: (1) In response to the changing State policy and market situation, the Group adjusted its operating strategy of the Trading Operations. While the existing products sold by the Group in the capacity of agent would continue, exploration of new products with market potential as well as expansion of distribution networks and markets beyond the province were actively pursued; (2) The Group enhanced the communication and cooperation with its suppliers to help them further expand the sales. In the meantime, while we continued our efforts in the sales of key products from large joint venture importers, we spent great efforts to look for and promote domestic non-patent protected medicines in a bid to ensure continuous growth of sales; (3) Measures were taken to improve credit control and receivable monitoring mechanism to minimize operations risks; (4) The Group continued to adjust to optimize its retail business. Diversification of products and expansion of product types would continue. New operating modes would be explored so as to enhance the market power of the Group and its products.

As of 31 December 2006, the Group had 142 retail chain pharmacies, including 86 "Cai Zhi Lin" which specialize in traditional Chinese medicines and 55 "Jian Min" which specialize in chemical medicines as well as one pharmacy named Ying Bang.



# Report of the Board of Directors

## MANAGEMENT DISCUSSION AND ANALYSIS (continued)

### (i) Business Scope and Analysis of Operations (continued)

#### 3. Details of operation and results of the Company's subordinated enterprises

Name	Major products and business nature	Percentage of direct holding of shares by the Company (%)	Sales income for the Year (RMB'000)	Profit for the Year (RMB'000)	Net profit for the Year (RMB'000)	Total assets as at the end of the Year (RMB'000)	Net assets as at the end of the Year (RMB'000)
Xing Qun Pharmaceutical	Manufacturing of CPM such as Xia Sang Ju	88.99	328,257	42,002	28,594	307,894	225,461
Zhong Yi Pharmaceutical	Manufacturing of CPM such as Xiao Ke Wan	100.00	651,876	124,770	84,205	490,958	419,268
Chen Li Ji	Manufacturing of CPM such as Wu Ji Bai Feng Wan	100.00	176,603	20,340	12,523	260,015	220,694
Guangzhou Qi Xing Pharmaceutical Co., Ltd	Manufacturing of CPM such as Hua Tuo Zai Zhao Wan	75.00	356,530	54,266	40,295	288,682	153,041
Jing Xiu Tang	Manufacturing of CPM such as Qing Re Xiao Yan Ning	88.40	207,295	17,295	17,295	171,274	123,097
Guangzhou Pan Gao Shou Pharmaceutical Co., Ltd ("Pan Gao Shou")	Manufacturing of CPM such as Mi Lian Chuan Bei Pi Pa Gao	87.77	271,620	22,531	16,800	283,124	194,547
Wang Lao Ji	Manufacturing of CPM such as Bao Ji Wan	48.0465	661,945	73,107	73,107	433,242	374,912
Guangzhou Huan Ye	Manufacturing of phytochemical medicine	100.00	34,794	163	57	43,884	24,199
Guangxi Ying Kang	Manufacturing of CPM such as Hua Tuo Feng Tong Bao	51.00	24,322	321	321	45,981	32,277
Guangzhou Bai Di	Research and development and manufacturing of bio-tech medicine	95.69	133	(12,779)	(12,779)	91,232	47,595
Guangzhou Han Fang	Research and development and manufacturing of CPM	70.04	6,539	(23,762)	(23,762)	170,822	73,609
Pharmaceuticals Corporation	Sales of chemical pharmaceutical products and medical apparatus	90.09	7,384,448	100,020	61,102	2,481,637	469,257
Chinese Medicine Corporation	Sales of Chinese raw medicine and CPM	100.00	1,093,020	(808)	(857)	440,693	19,265
Guangzhou Pharmaceutical Import & Export Corporation ("Pharmaceutical Import & Export Corporation")	Import and export of TCM and chemical medicine	100.00	321,042	3,462	1,841	110,766	23,892
Ying Bang Company	Sales of Chinese raw medicine, CPM and materials	51.00	29,206	(560)	(621)	8,465	7,036

Note: The operating results and assets of Wang Lao Ji as stated in the above chart were stated according to the respective figures of the whole Company.

None of the Group's invested companies derived to the Group of any investment income, which equals to 10% or more of the Group's net profit.

#### 4. Major customers and suppliers

During the Year, purchases of goods and services from the 5 largest suppliers amounted to RMB1,234,951,000, representing approximately 14.33% of the total purchases. The purchases from the largest supplier amounted to RMB313,092,000, representing 3.63% of the total purchases. Goods and services sold to the 5 largest customers amounted to RMB798,426,000, representing 7.80% of the total sales. Sales to the largest customer amounted to RMB257,472,000, representing 2.51% of the total sales of the Group.

To the knowledge of the Board, none of the Directors, their associates or shareholders holding more than 5% of the Company's total issued share capital had any interest in any of the 5 largest suppliers or customers noted above.



# Report of the Board of Directors

## MANAGEMENT DISCUSSION AND ANALYSIS *(continued)*

### (II) The possible changes of accounting policies and accounting estimates of the Group after carrying out new Accounting Standards for Enterprises and their effects to financial conditions and operating results of the Group

From 1 January 2007, the Group applies new Accounting Standards for Business Enterprises. A detailed analysis of its effect on the accounting policies, accounting estimates and the financial position and results from operations of the Group are set out as follows:

1. Scope of consolidated financial statements: the interests in joint ventures are no longer proportionally consolidated. Instead, equity method is used for consolidation. In 2006 and previous years, proportional consolidation method was used for consolidating financial statements of joint ventures such as Wang Lao Ji based on the shareholding attributable to the Group. In accordance with "Accounting Standards for Business Enterprise No. 33 — Consolidated Financial Statements" and "Accounting Standards for Business Enterprises No.2 — Long-term Equity Investment", equity method will be used for long-term investments in joint ventures and such investments will no longer be consolidated since the year 2007. The change of this accounting policy will affect the results from operations of the Group recorded in the consolidated financial statements, meaning that the profit of the owners of the Company will be affected. For example, for the 2006 consolidated financial statements of the Group, in accordance with the new accounting principles, the total assets recorded in the consolidated balance sheet would be decreased by approximately 0.52% when compared with the original balance sheet. The principal operations income and the relevant costs in the consolidated income statement would be decreased by 1.29% and 1.56% correspondingly while the net profit would be increased by 0.51%.
2. As of 31 December 2006, the Group separately assessed the value of its investment properties in accordance with the "Accounting Standards for Business Enterprises No. 3 — Investment Property" and adopted the cost method for the additional supplementary calculation with the absence of retrospective adjusted items.
3. The financial statements of the Group on the first adoption date involves such modified accounting policies with retrospective effect as "Accounting Standards for Business Enterprises No. 2 — Long-term Equity Investment", "Accounting Standards for Business Enterprises No. 13 — Contingent Events", "Accounting Standards for Business Enterprises No. 18 — Income Tax", "Accounting Standards for Business Enterprises No. 20 — Business Combination".
  - (1) Take the 2006 income statements as an example, the effect on the results from operation resulting from such changes of accounting principles would be reflected by an increase of RMB6,243,000 in consolidated net profit in 2006, representing a net increase of 2.75% in profit when compared with the original income statement. Among which, an increase in the deferred income tax assets would result in a decrease of RMB1,059,000 in net profit. Such changes of accounting policies would not significantly affect the results from operations of the Group.
  - (2) The retrospective adjustment to relevant transactions and matters resulting from the changes of accounting policies will result in an increase of RMB2,276,000 in the shareholders' funds in the Company, representing approximately 0.08% of net assets as at 31 December 2006. Among which, an increase in the deferred income tax assets will result in an increase of RMB60,644,000 in the retained profit. An increase in the estimated liabilities of employee benefits in medical insurance will result in a decrease in the retained profit by RMB55,071,000. Because of the effects of the new standards (which change the scope of consolidation), the retained profit declined by RMB 100,000. The debit balance of long-term equity investments will result in a decrease in the retained profit by RMB2,285,000. The written off of the remaining value of the goodwill will result in a decrease of RMB912,000 in the retained profit. The retrospective adjustment to such accounting policies will not significantly affect the shareholder's funds of the Group.



# Report of the Board of Directors

## MANAGEMENT DISCUSSION AND ANALYSIS *(continued)*

### (II) The possible changes of accounting policies and accounting estimates of the Group after carrying out new Accounting Standards for Enterprises and their effects to financial conditions and operating results of the Group *(continued)*

- The accounting estimates adopted by the Group include depreciable life of fixed assets, depreciable life of investment properties, amortization period of land use right of the intangible assets. The adoption of new "Accounting Standards for Business Enterprises" will not result in a change of such accounting estimates.

In conclusion, the adoption of the new "Accounting Standards for Business Enterprises" mainly affects the consolidated scope of the consolidated financial statements of the Group. Accounting estimates, the financial position and results from operations of the Group will not be significantly affected.

### (iii) The Company's Investments

- Use of proceeds from the issue of A shares during the Reporting Period

The Company issued 78,000,000 A shares at the issue price of RMB9.80 per share in the PRC on 10 January 2001. The net proceeds raised from the issue of A shares were RMB737,990,000. The portion exceeding the budgeted proceeds amounting to approximately RMB29,690,000 was used as supplemental working capital. As at 31 December 2006, an aggregate of RMB695,540,000 of the proceeds from the issue of A shares were utilised. The remaining unused proceeds amounting to RMB42,450,000 are currently used as working capital. As at the end of the Reporting Period, the use of proceeds from the issue of A shares was in line with the undertakings made in the prospectus for the issue of A shares. Save as the following items, proceeds were invested as scheduled.

Category	Projects	Budgeted injection from the proceeds (RMB'000)	Accumulated amount injected as at the end of the Reporting Period (RMB'000)	Stage of completion (%)
Pills	Industrialization of Wei Re Qing	29,000	25,960	93
	Technology upgrade of throat, spleen and intestine pills	29,100	25,830	95
Tablets	Industrilisation of Fu Yan Soluble Tablets	29,500	24,060	90
Expansion of chain pharmacies	Cai Zhi Lin	59,500	29,260	70

#### (1) Explanatory note on return on projects and delay in completion of certain projects

During the Reporting Period, additional sales and gross profit from the issue of A Shares amounted to RMB 4,267,410,000 and RMB 604,620,000 respectively.

Among these, projects such as Fu Yan Soluble Tablets and Wei Re Qing Capsules were postponed because of market changes, and the expansion of chain pharmacies had slowed down as a result of keen competition in the domestic pharmaceutical market.

#### (2) As of 31 December 2006, there was no change in the actual application of the proceeds of the issue of A shares.



# Report of the Board of Directors

## MANAGEMENT DISCUSSION AND ANALYSIS *(continued)*

### (iii) The Company's Investments *(continued)*

#### 2. Other investment projects during the Reporting Period

Content	Date	Amount	Stage
Guangzhou Bai Di, a subsidiary of the Company, cancelled the Agreement in relation to Capital Contribution for Establishment of Guangzhou Huayin Bio-tech Co., Ltd (廣州華因生物技術有限公司), and withdrew its original investment RMB 1 million, and relevant dissolution and liquidation were completed in accordance with the relevant procedures.	27 January 2006	RMB1,000,000	Completed
Guangzhou Bai Di, a subsidiary of the Company, and Guangzhou Jiahe Bio-tech Co., Ltd (廣州市嘉合生物技術有限公司) jointly set up Guangzhou Nuocheng Bio-technology Co., Ltd. (廣州諾誠生物製品股份有限公司)	27 January 2006	RMB6,000,000	Completed
Guangzhou Bai Di, a subsidiary of the Company, increased investment and shares in Guangzhou Nuocheng Bio-technology Co., Ltd	26 September 2006	RMB10,000,000	Completed



### (iv) Analysis of Financial Conditions

#### 1. Financial conditions of the Group

*Prepared in accordance with PRC accounting standards and systems*

Items	As at 31 December 2006 (RMB'000)	As at 31 December 2005 (RMB'000)	Change (%)
Total assets	5,409,413	5,098,095	6.11
Shareholders' funds	2,788,088	2,621,437	6.36
Profit from principal activities	1,743,185	1,528,752	14.03
Net profit	227,328	184,482	23.23
Net increase/(decrease) in cash and cash equivalents	(127,855)	(263,842)	51.54



# Report of the Board of Directors

## MANAGEMENT DISCUSSION AND ANALYSIS *(continued)*

### (iv) Analysis of Financial Conditions *(continued)*

#### 1. Financial conditions of the Group *(continued)*

##### *Prepared in accordance with HKFRS*

Items	As at 31 December 2006 (RMB'000)	As at 31 December 2005 (RMB'000)	Change (%)
Total assets	5,640,964	5,316,420	6.10
Capital and reserves attributable to equity holders of the Company	2,897,389	2,723,123	6.40
Profit before income tax	349,155	315,493	10.67
Profit attributable to equity holders of the Company	218,067	197,804	10.24
Net increase/(decrease) in cash and cash equivalents	(129,453)	(263,804)	50.93

#### 2. Liquidity

As at 31 December 2006, the current ratio of the Group was 1.60 (31 December 2005: 1.55), and its quick ratio was 1.04 (31 December 2005: 0.98). Accounts receivable turnover rate was 10.35 times, representing a decrease of 5.59% as compared with that of 2005. Inventory turnover rate was 6.85 times, representing an increase of 1.99% as compared with last year.

#### 3. Financial resources

As at 31 December 2006, cash and cash equivalents of the Group amounted to RMB489,128,000, out of which 95.97% and 4.03% were denominated in Renminbi and foreign currencies, like Hong Kong dollars, respectively.

As at 31 December 2006, the Group had bank borrowings of RMB888,199,000 in total, all of which were short-term borrowings (31 December 2005: RMB867,785,000).

#### 4. Capital structure

As at 31 December 2006, the Group's current liabilities amounted to RMB2,384,082,000 (31 December 2005: RMB2,236,332,000), representing an increase of 6.61% over that of 2005, and its long-term liabilities was RMB71,154,000 (31 December 2005: RMB54,826,000), with an increase of 29.78% as compared with 2005. The shareholders' funds amounted to RMB2,788,088,000 (31 December 2005: RMB2,621,437,000), with an increase of 6.36% as compared with 2005.

#### 5. Capital expenditure

The Group expects the capital expenditure for 2007 to amount to approximately RMB227 million (2006: RMB102 million), which will be mainly applied in the construction of factories and infrastructure and acquisition of machines and equipment, etc. The Group has sufficient financial resources to meet the capital expenditure and daily working capital requirements.

#### 6. Gearing ratio

As at 31 December 2006, the Group's gearing ratio (calculated according to the formula: total liabilities/total assets) was 45.39% (31 December 2005: 44.94%), with an increase of 0.45 percentage point as compared with the year 2005.



# Report of the Board of Directors

## MANAGEMENT DISCUSSION AND ANALYSIS *(continued)*

### (iv) Analysis of Financial Conditions *(continued)*

#### 7. Exposure to fluctuations in exchange rates

As majority of the revenue, expenses, assets and liabilities of the Group are denominated or settled in Renminbin, the Group does not have significant risks in exposure to fluctuations in exchange rates.

#### 8. Main cash resources and applications

As of 31 December 2006, cash and cash equivalents of the Group amounted to RMB489,128,000, with a decrease of RMB127,855,000 as compared with last year. The net cash inflow delivered from operating activities amounted to RMB38,880,000, with a decrease of RMB107,442,000 as compared with last year, which was mainly attributable to the increase of accounts receivable, notes receivable and inventory for the Year.

#### 9. Contingent liabilities

As of 31 December 2006, the Group has no significant contingent liabilities.

#### 10. Charge on the Group's assets

At 31 December 2006, the Group's bank loans were secured by fixed assets with a net book value of RMB54,970,000.

### (v) Impact caused by the changes in operation environment and national macro economic policy on the Group

Factors such as the changes of the national policy regarding the prices of pharmaceutical products, the increased prices of raw materials and ancillary materials, the increased production cost resulting from GMP renovation of the Group's Manufacturing Operations and lower gross profit margin of the Trading Operations have caused certain impact on the Group's operating results.

### (vi) The annual financial reports of the Group and the Company for the year of 2006 have been audited and signed by Guangdong Yangcheng Certified Public Accountants Co., Ltd, the PRC auditors, and PricewaterhouseCoopers, the international auditors, who have both issued unqualified auditors' reports thereon.

### (vii) Prospects and Plans for 2007

In 2007, the Group will focus on strengthening management in the base-level, continue the brand-oriented strategy, and further consolidate its resources. Efforts will be spent on exploring new products with market potential and new markets so as to increase the core competitiveness of the Group, and thus achieve sustainable and stable growth.

The plans for 2007 mainly include:

1. To expedite technology innovation by increasing research and development of products including modern Chinese medicines, phytochemical extracts and biological vaccines and to aggressively facilitate the industrialization of technological achievements so as to enhance the Group's competitive edge.



# Report of the Board of Directors

## MANAGEMENT DISCUSSION AND ANALYSIS *(continued)*

### (vii) Prospects and Plans for 2007 *(continued)*

2. To continue to strengthen the promotion efforts of the Group's corporate brands and product brands with focus on the core products such as Zhong Yi Xiao Ke Wan, Wang Lao Ji Liang Cha, Xing Qun Xia Sang Ju, Qi Xing Hua Tuo Zai Zao Wan and Pan Gao Shou Chuan Bei Pi Pa Series, while promoting new products such as Kun Xian Capsule, Ganoderma Lucidum Spore Oil and rabies vaccines, with a view to create certain new growth drivers.
3. To continue to expedite integration of internal resources within the Group and to centralize the purchase raw materials in large bulks, packing materials and import materials, as well as to strengthen the co-operation between its manufacturing and trading enterprises within the Group and financial management and the Group's effectiveness.
4. To aggressively seek opportunities for cooperation with outstanding pharmaceutical enterprises and research institutions at home and abroad, making use of their strength to facilitate the development of the Company's core business.
5. To continue to improve fundamental management capabilities through perfecting corporate governance system and setting up and improving internal control system and management procedures, promoting better internal communication as well as fine-tuning internal control and review system. Hence, operating risks can be lower and the Group's operations satisfied the required standards.

The Company will face both new opportunities and challenges in 2007. Both management and the staff will continue to exercise the spirit of industry, progress, pragmatics and innovation with all efforts so as to achieve a rapid, sustainable and healthy growth for the Group and thus generate a better return for our shareholders.



# Report of the Board of Directors

## DAILY OPERATIONS OF THE BOARD

### (i) Board Meetings

Meetings	Date of meeting	Resolutions	Newspapers on which the resolution was published	Publication dates of the resolutions
19th meeting of the Third Session	23 February 2006	/	Shanghai Securities, Hong Kong Economic Times and The Standard in Hong Kong	24 February 2006
20th meeting of the Third Session	27 April 2006	(1) Upon the authorization and acting on behalf of GPL, agree to convene relevant A shareholders' meeting to review its proposed share reform plan; (2) Agree to solicit the votes of the A shareholders of circulating shares of the Company in respect of the share reform plan; (3) Upon the authorization and acting on behalf of GPL, agree to prepare explanatory statement relating to the share reform and all other necessary documents, and assist in implementing other necessary procedures to support the share reform of the Company; (4) Authorize Xie Bin, the Director, to execute the relevant documents, and to do such things and acts and execute such documents which he considers necessary or expedient for the support of the share reform of the Company.	/	/
21st meeting of the Third Session	31 March 2006	/	Shanghai Securities, Hong Kong Economic Times and The Standard in Hong Kong	3 April 2006
22nd meeting of the Third Session	27 April 2006	/		28 April 2006
23rd meeting of the Third Session	15 June 2006	/		16 June 2006
24th meeting of the Third Session	26 July 2006	/		27 July 2006



# Report of the Board of Directors

## DAILY OPERATIONS OF THE BOARD *(continued)*

### (i) Board Meetings *(continued)*

Meetings	Dates	Resolutions	Newspapers on which the resolution was published for	Publication dates of the resolution
25th meeting of the Third Session	25 August 2006	/	Shanghai Securities, Hong Kong Economic Times and The Standard	28 August 2006
26th meeting of the Third Session	26 October 2006	/		27 October 2006
27th meeting of the Third Session	13 December 2006	The resolution on the remuneration of Independent Non-executive Directors and external supervisors for the year 2006 was considered and passed	/	/
28th meeting of the Third Session	13 December 2006	The resolution on the authorization to execute the relevant documents in connection with the application for E-Submission System separate account to HKEX was proposed.	/	/



### (ii) The progress of execution by the Directors in respect of the resolutions passed at general shareholders' meetings

#### 1. Distribution of 2005 final dividend

Pursuant to the resolution passed at the 2005 AGM, a final dividend of RMB0.07 per share (including withholding tax for A shares) for 2005 had been paid to the Company's shareholders by July 2006. The registration date for the entitlement of holders of H shares to the final dividend was 16 May 2006, while the book closing date was 17 May 2006. The registration date for the entitlement of holders of A shares to the final dividend was 29 June 2006 and the book closing date was 30 June 2006.

#### 2. Proposed scheme of profit distribution and increase in share capital by transfer from capital reserve

The amount of retained profits available for the distribution to shareholders of the Company is the lower of the amount determined in accordance with PRC Accounting Standards and Systems and the amount determined in accordance with HKFRS. The Board recommended a final dividend of RMB0.084 per share (including withholding tax for A shares) for the year ended 31 December 2006 (2005: RMB0.07). The proposed final dividend will be submitted to the forthcoming 2006 AGM for consideration and approval.

During the Year, there was no increase in share capital from the capital reserve.

# Report of the Board of Directors

## OTHER MATTERS

### (i) Accounts

The results of the Group for the year ended 31 December 2006 are set out in the consolidated income statement prepared in accordance with PRC Accounting Standards and Systems and HKFRS on page 56 and page 140, respectively.

The financial conditions of the Group as at 31 December 2006 are set out in the consolidated balance sheet prepared in accordance with PRC Accounting Standards and Systems and HKFRS on page 54 and page 138, respectively.

The cash flows of the Group for the year ended 31 December 2006 are set out in the consolidated cash flow statement prepared in accordance with PRC Accounting Standards and Systems and HKFRS on page 59 and page 142, respectively.

The cash flows of the Company for the year ended 31 December 2006 are set out in the cash flow statement prepared in accordance with PRC Accounting Standards and Systems on page 68.

### (ii) Financial Summary

A summary of the results and of the assets and liabilities of the Group for the last five financial years prepared in accordance with HKFRS is set out on page 5.

A summary of the results and of the assets and liabilities of the Group for the last three financial years prepared in accordance with PRC Accounting Standards and Systems is set out on page 4.

### (iii) Reserves

Details of movements in the reserves of the Group during the year prepared in accordance with PRC Accounting Standards and Systems are set out on pages 107 to 108. Details of movements in the reserves of the Group during the year prepared in accordance with HKFRS are set out on pages 173 to 175.

### (iv) Distributable Reserves

The profit available for distribution to shareholders is the lower of the amount determined in accordance with HKFRS and the PRC Accounting Standards and Systems. The distributable reserves of the Group as at 31 December 2006 amounted to RMB175,905,000, calculated in accordance with the PRC Accounting Standards and Systems and amounted to RMB219,869,000 calculated in accordance with HKFRS.

### (v) Fixed Assets

Details of the movements of fixed assets for the year are set out on pages 89 and pages 163 to 165 herein.



# Report of the Board of Directors

## OTHER MATTERS *(continued)*

### (vi) Continuing Connected Transactions

Pursuant to the regulations of CSRC, details of the connected transactions were set out on pages 118 to 127 herein.

Pursuant to the rules of HKEx, details of the connected transactions were set out as follows:

	<b>2006</b> <b>(RMB'000)</b>
Ultimate holding company	
License fee expense	<b>10,782</b>
Service fee expense	<b>939</b>
Welfare facilities fee expense	<b>274</b>
Rental expense	<b>2,944</b>
Fellow subsidiaries	
Sales of finished goods and raw materials	<b>196,786</b>
Purchase of finished goods and raw materials	<b>555,962</b>
Advertisement expenses	<b>19,144</b>

In addition, other transactions with jointly controlled entities and associated companies which, pursuant to the Listing Rules of HKEx, do not constitute connected transactions, have been disclosed in notes to the financial reports prepared in accordance with HKFRS.

The Directors believe that the above-mentioned connected transactions have been conducted in full compliance with the relevant clauses governing such transactions stipulated in the Agreement in relation to the Sales and Purchase Connected Transactions (as amended) entered into between the Company and GPLH on 27 April 2005 and the Agreement in relation to the Advertisement Continuing Connected Transactions entered into between the Company and GPSC on 15 June 2006.

The Independent Non-Executive Directors have reviewed the connected transactions and regarded all the transactions as being carried out within the Company's ordinary operations and under ordinary business terms. Such terms were considered normal business terms or terms to the Company no less favourable than those available to or from independent third parties. In addition, the aggregate amount of the above connected transactions during the year has not exceeded the annual caps as stated in the Agreement in relation to the Sales and Purchase Connected Transactions (as amended) entered into between the Company and GPLH or in the Agreement in relation to the Advertisement Continuing Connected Transactions entered into between the Company and GPSC.

The international auditors have confirmed that continuing connected transactions out of the above transactions pursuant to the Listing Rules of HKEx:

- had been approved by the Board of Directors of the Company;
- were entered into in accordance with the relevant pricing policies;
- were entered into in accordance with the terms of the relevant agreements governing such transactions; and
- have not exceeded the annual caps as stated in the Agreement in relation to the Sales and Purchase Connected Transactions (as amended) entered into between the Company and GPLH or in the Agreement in relation to the Advertisement Continuing Connected Transactions entered into between the Company and GPSC.



# Report of the Board of Directors

## OTHER MATTERS *(continued)*

### (vii) Management Contracts

No contracts concerning the management and administration of the whole or any substantial part of the business of the Company were entered into or existed during the year.

### (viii) Compliance with the Code on Corporate Governance Practices

Throughout the year, the Company was in compliance with the code provisions set out in the Code on Corporate Governance Practices contained in Appendix 14 to the Listing Rules of HKEx.

### (ix) Audit Committee

The Audit Committee had reviewed the accounting principles, accounting standards and methods adopted by the Group, and had discussed with the management about the audit, internal controls and financial reporting. The Committee also reviewed the audited annual accounts of the Group and the Company for the year ended 31 December 2006.

### (x) Tax Exemption

Pursuant to Document Guo Shui Fa [1993] No. 045 issued by the State Administration of Taxation, individual foreigners in the PRC are exempt from income tax on dividend incomes derived from holdings shares in companies listed on overseas stock exchanges, including H shares. Except for the above, there is no other tax preferential scheme.

### (XI) Retirement Scheme

Details of the retirement scheme and amounts of contributions of the Group charged to the profit and loss account for the year are set out on page 182, respectively.

### (XII) Staff Quarters

Pursuant to the Accommodation Service Agreement entered into between the Company and GPHL, GPHL agreed to sell the staff quarters to the employees of the Group at a preferential price. The Company shall pay to GPHL the staff quarters reform costs, which represent the difference between the preferential price and the cost net of accumulated depreciation paid by GPHL on construction or acquisition of such staff quarters. As at 31 December 2006, the total staff quarters reform costs, which are payable to GPHL, amounted to approximately RMB61,655,000 (31 December 2005: RMB61,655,000).

In addition, the Group has constructed or acquired certain staff quarters. As at 31 December 2006, the difference between the construction cost or acquisition cost and the revenue from disposal of the quarters totaled RMB42,437,000 (31 December 2005: RMB42,437,000).

Correspondingly, the above-mentioned staff quarters reform costs amounted to RMB104,092,000 as at 31 December 2006 (2005: RMB104,092,000). According to the Document Cai Qi [2000] No.29, the Notice on Accounting Treatment of Housing Reform Initiated in Enterprises, issued by the Ministry of Finance, the costs arising therefrom should be dealt with in retained earnings as at 1 January 2006 under the statutory accounts. Subject to the approval by the Board of Directors, any deficit balance resulting therefrom should be appropriated to the statutory public welfare fund, statutory surplus reserve fund, and capital reserve. This accounting treatment has been adopted in the financial statements prepared in accordance with the PRC Accounting Standards and Systems.





# Report of the Board of Directors

## OTHER MATTERS *(continued)*

### (XII) Staff Quarters *(continued)*

For the financial statements prepared in accordance with HKFRS, the staff quarters reform costs have been deferred and amortized on a straight-line basis to the profit and loss account over a period of 10 years, which is the estimated remaining average service life of the employees. The total accumulated amortization as at 31 December 2006 was approximately RMB77,086,000, and the amortization for 2006 was RMB10,361,000. As at 31 December 2006, the balance of such deferred staff quarters reform costs was RMB27,006,000. In the opinion of the Board of Directors of the Company, if the aforesaid balance of deferred staff quarter reform costs had been completely written off in 2006, the total assets of the Company as at 31 December 2006 would have been reduced by approximately RMB27,006,000. With respect to the document Sui Fu [2000] No. 18 issued by the Guangzhou People's Municipal Government concerning the one-time cash accommodation allowance to those employees to whom the Group has not allocated staff quarters and those aged employees whose allocated staff quarters do not meet required standards, the Directors consider that the said document is not legally binding on the Group. Since 2001, the Group has formulated its own cash accommodation allowance policy to employees based on the situation of the entities within the Group.

### (XIII) Projects under Development and for Sale

During the Reporting Period, the Group did not hold any properties for the purpose of development and/or for sale or investment, of which the amounts are above 5% of the net tangible assets of the Group or the contribution to profit before tax from these properties is over 5% of the Group's total profit before tax.

### (XIV) Bank Loans, Overdrafts and Other Loans

Details of the bank loans, overdrafts, and other liabilities of the Group as at 31 December 2006 are set out on pages 102 to 105. In comparison to last year, there have been no material adverse changes in respect of the amounts of bank loans, short-term borrowings and total liabilities as of 31 December 2005.

### (XV) Auditors

Guangdong Yangcheng Certified Public Accountants Co., Ltd. and PricewaterhouseCoopers were respectively re-appointed as domestic and international auditors of the Company for the year 2006, as approved at the 2005 AGM.

There was no change in auditors in the past 3 years.

### (XVI) Changes in the Newspapers Designated by the Company for Information Disclosure

During the Reporting Period, there was no change in the newspapers designated by Company for information disclosure.

### (XVII) Explanation of Certified Public Accountants in respect of Funds Appropriated by the Controlling Shareholder and Other Connected Parties of the Company

Guangdong Yangcheng Certified Public Accountants Co., Ltd., the PRC auditors of the Company, has made an explanation in respect of the funds appropriated by the controlling shareholder and other connected parties of the Company.



# Report of the Board of Directors

## OTHER MATTERS (continued)

### (XVII) Explanation of Certified Public Accountants in respect of Funds Appropriated by the Controlling Shareholder and Other Connected Parties of the Company (continued)

In accordance with the requirements as set out in the Document Zheng Jian Fa [2003] No. 56, Notice Concerning the Regulation on the Flow of Funds between Listed Companies and their Connected Parties and the Provision of Guarantees by Listed Companies to External Parties issued by the CSRC and the State Asset Management Commission under the State Council, a statement on the application of funds by the Company's controlling shareholders and other connected parties for the year ended 31 December 2006 has been prepared and is set out below:

Name of the party who used the Funds	The relationship between the party and the listed company	The account item for the amount will be included	The fund appropriated at the beginning of 2006 (RMB'000)	Accumulated amount appropriated in 2006 (RMB'000)	Accumulated amount repaid in 2006 (RMB'000)	Fund appropriated as at the end of 2006 (RMB'000)	Reasons	Nature
GPHL	Parent Company	Other receivables	5,060	86	1,075	4,071	Prepaid rentals and daily transactions	Operational
Guangzhou Baiyunshan Qiao Guang Pharmaceutical Co., Ltd	With the same ultimate holding company	Account receivables	26,468	69,600	61,301	34,767	Payment for goods	Operational
Guangzhou Ming Xing Pharmaceutical Co., Ltd	With the same ultimate holding company	Account receivables	1,714	21,370	22,002	1,082	Payment for goods	Operational
		Prepayment	—	8,547	171	8,376	Payment for goods	Operational
Guangzhou Tian Xin Pharmaceutical Co., Ltd	With the same ultimate holding company	Account receivables	1,842	13,082	13,511	1,413	Payment for goods	Operational
		Prepayment	—	1,543	—	1,543	Payment for goods	Operational
Guangzhou He Ji Gong Pharmaceutical Co., Ltd	With the same ultimate holding company	Account receivables	238	4,641	4,179	700	Payment for goods	Operational
		Prepayment	—	1,656	1,527	129	Payment for goods	Operational
Guangzhou Baiyunshan Guang Hua Pharmaceutical Co., Ltd	With the same ultimate holding company	Account receivables	2,895	58,459	54,452	6,902	Payment for goods	Operational
		Prepayment	—	18,748	10,000	8,748	Payment for goods	Operational
Guangzhou Hua Nan Medical Apparatus Co., Ltd	With the same parent company	Other receivables	100	—	—	100	Payment for goods	Operational
Po Lian Development Co., Ltd	With the same parent company	Other receivables	7,993	—	7,993	—	Payment received on behalf of third party	Non-operational parent company
		Prepayment	—	9,369	—	9,369	Payment for goods	Operational
Guangzhou Medical Industrial Research Institute	With the same parent company	Account receivables	—	8	8	—	Payment for goods	Operational
Guangzhou Baiyunshan HW Chinese Medicine Co., Ltd	With the same ultimate holding company	Account receivables	1,777	13,408	14,491	694	Payment for goods	Operational
		Prepayment	197	342	193	346	Payment for goods	Operational



# Report of the Board of Directors

## OTHER MATTERS *(continued)*

### (XVII) Explanation of Certified Public Accountants in respect of Funds Used by the Controlling Shareholders and Other Connected Parties of the Company *(continued)*

Name of the party who used the Funds	The relationship between the party and the listed company	The account item for the amount will be included	The fund appropriated at the beginning of 2006 RMB'000	Accumulated amount appropriated in 2006 RMB'000	Accumulated amount repaid in 2006 RMB'000	Fund appropriated as at the end of 2006 RMB'000	Reasons for drawing fund	Nature
Guangzhou Baiyunshan Pharmaceutical General Factory-	With the same ultimate holding company	Account receivables	4,225	31,020	31,326	3,919	Payment for goods	Operational
Guangzhou Baiyunshan Chemical Medicine Factory	With the same ultimate holding company	Account receivables	1,209	16,063	14,005	3,267	Payment for goods	Operational
Guangzhou Baiyunshan External Use Pharmaceutical Co., Ltd.	With the same ultimate holding company	Account receivables	170	2,563	1,875	858	Payment for goods	Operational
Guangzhou Pharmaceutical Economic and Development Corporation	With the same parent company	Account receivables	—	26	—	26	Payment for goods	Operational
Wang Lao Ji	Joint venture	Account receivables	2,268	47,027	48,786	509	Payment for goods	Operational
		Other receivables	—	362	—	362	Trademark fees	Operational
Guangzhou Lianjie Computer Technology Co., Ltd	Joint venture	Other receivables	520	—	520	—	Current borrowings	Non-Operational
Sub-total		Account receivables	42,805	277,266	265,936	54,135		
		Other receivables	13,673	448	9,588	4,533		
		Prepayment	197	40,204	11,891	28,510		



# Report of the Board of Directors

## (OTHER MATTERS (continued))

### XVIII) Explanation and Independent Opinions of Independent Directors in respect of Accumulated and Current Guarantees to External Parties Granted by the Company and the Funds Appropriated by the Controlling Shareholders and Other Connected Parties of the Company

Based on the principle of de facto and pursuant to the principle as implied in the Document Zheng Jian Fa [2003] No. 56, Notice Concerning the Regulation on the Flow of Funds between Listed Companies and their Connected Parties and the Provision of Guarantees by Listed Companies to External Parties, the Independent Directors of the Company have conducted examination of the policies towards the guarantees provided to the external parties by the Group in a serious manner. The relevant details are as follows:

As at 31 December 2006, the Company had provided the following guarantees to its subsidiaries:

Guaranteed Party	Guarantee amount (RMB'000)	Subject matter	Guarantee period
Pharmaceuticals Corporation	220,000	Current borrowings	One year
Chinese Medicine Corporation	10,000	Current borrowings	One year
Pharmaceutical Import & Export Corporation	10,000	Current borrowings	One year
Guangzhou Han Fang	34,920	Current borrowings	One year
Guangzhou Bai Di	10,000	Current borrowings	One year
Pharmaceuticals Corporation	60,630	Discounted note	One year
Pharmaceutical Import & Export Corporation	8,970	Discounted note	One year
Pharmaceutical Import & Export Corporation	9,560	Discounted note	One year
	<u>364,080</u>		

As at the end of this Reporting Period, the Group has not provided any guarantee to its controlling shareholder and any other connected parties.

On behalf of the Board  
**Yang Rongming**  
Chairman

Guangzhou, the PRC, 27 April 2007



# Report of the Supervisory Committee

To all shareholders:

On behalf of the supervisory committee of the Company (the "Supervisory Committee"), I hereby report to you the duties performed by the Supervisory Committee during the year ended 31 December 2006 in accordance with the Company's Articles of Association.

## (I) MEETINGS OF THE SUPERVISORY COMMITTEE HELD DURING THE YEAR

During the Reporting Period, four meetings were held.

Session and number of meeting	Date of meeting	Resolutions	Newspapers for publication of resolutions	Dates for publication of resolutions
7th meeting of the Third Session	31 March 2006	The following resolutions were considered and passed: text and summary of 2005 annual report of the Company, report of the Supervisory Committee for the year 2005, financial reports of the Company for the year 2005 and provision of guarantees by the Company to secure bank loans for its certain subsidiaries in 2006.	Shanghai Securities in the PRC, Hong Kong Economic Times and The Standard in Hong Kong	3 April 2006
8th meeting of the Third Session	27 April 2006	1st quarterly report of 2005 of the Company and amendments to the Rules of Procedures for the Supervisory Committee of the Company were considered and passed.	/	/
9th meeting of the Third Session	25 August 2006	Interim report and interim financial report of the Company for the year 2006 were considered and passed.	/	/
10th meeting of the Third Session	26 October 2006	3rd quarterly report of 2006 of the Company was considered and passed.	/	/

## (II) INDEPENDENT OPINION OF THE SUPERVISORY COMMITTEE ON THE COMPANY'S OPERATIONS

### 1. The Company's operations during the Reporting Period

During the Reporting Period, the Supervisory Committee has monitored the procedures for convening Board meetings and shareholders' meetings and the resolutions proposed to be considered thereat, as well as the execution by the Board of the resolutions passed at the shareholders' meetings and has no dissenting view on any reports and proposals submitted by the Board at shareholders' meetings. The Supervisory Committee considers that during the Reporting Period the operations conducted by the Company are in compliance with the Company Law, the Securities Law, the respective Listing Rules governing the securities exchanges in PRC and in Hong Kong, the Articles of Association and other relevant laws and regulations, and the Company has executed the resolutions of the shareholders' meetings of the Company diligently, continued to enhance the internal management and internal control systems of the Company and established a good internal management system. The Company's Directors and Senior Management have not committed any acts in breach of the rules and regulations, the Articles of Association, nor have they engaged in any acts involving the infringement of the Company's interest or infringement of shareholder's interests.



# Report of the Supervisory Committee

## (II) INDEPENDENT OPINION OF THE SUPERVISORY COMMITTEE ON THE COMPANY'S OPERATIONS *(continued)*

### 2. The supervision of the Company's financial conditions

The Supervisory Committee has carefully reviewed the financial statements and other financial information of the Company during the Reporting Period, and considers that the Company's financial statements are fairly presented, and the auditing and financial management are in line with the relevant regulations. The domestic and international auditors issued their standard and unqualified auditors' reports upon auditing the accounts of the Group and the Company for the year ended 31 December 2006, which reflect an objective, true and fair view of the financial status of the Company as at 31 December 2006 and the operations results of the Group for the year then ended.

### 3. Use of proceeds raised from the issue of A shares

During the Reporting Period, the use of the proceeds from the issue of A shares was in line with the undertakings made in the prospectus for the issue of A shares. There was no improper use of the proceeds.

### 4. Purchases and sales of assets of the Company

During the Reporting Period, the considerations for purchases and sales of assets are reasonable and arrived at on an arm's length basis. There has been no insider dealings which would harm the interests of certain shareholders or cause loss of the Company's assets.

### 5. Connected transactions

During the Reporting Period, the Company's connected transactions mainly include:

Certain entities under the Company and BYSCL together with some of its subsidiaries jointly contributed for the establishment of GPSC.

The Continuing Connected Transaction of Advertising Agreement entered into between the Company and GPSC which governs the daily advertising between both parties.

The above connected transactions are arrived at on an arm's length basis and do not involve any actions which may adversely affect the interests of the Company and its shareholders.

On behalf of the Supervisory Committee  
**Chen Canying**  
*Chairman*

Guangzhou, the PRC, 27 April 2007



## Other Events

### (I) SIGNIFICANT LITIGATION OR ARBITRATION

The Group had no significant litigation or arbitration during the Reporting Period.

### (II) THE COMPANY'S PURCHASE AND DISPOSAL OF ASSETS (INCLUDING SUBSIDIARIES OR ASSOCIATED COMPANIES) OR MERGER AND ACQUISITION ACTIVITIES DURING THE REPORTING PERIOD

The Company entered into an equity transfer agreement with Hong Kong Xin Lian Hua Industrial Company Limited ("Xin Lian Hua") on 24 March 2006 in respect of a transfer of the 21.42% shareholding of the Company in Nanfang Packaging Co., Limited (佛山市南方包装有限公司) to Xin Lian Hua at a consideration of RMB30,000,000. The equity transfer was completed.

### (III) CONNECTED TRANSACTIONS

1. Certain entities under the Company and Baiyunshan Co., Ltd together with six of its subsidiaries agreed to contribute jointly RMB20,000,000 in cash for the establishment of GPSC. On 23 February 2006, the parties entered into an Agreement for the Establishment of GPSC. According to the respective listing rules of SSE and HKEx, the transaction constituted a connected transaction. The agreement was considered at the 19th meeting of the Third Session of the Board held on 23 February 2006, and in respect of which, the Independent Non-executive Directors expressed their independent opinion.

For details, please refer to the announcements published in Shanghai Securities in the PRC, and Hong Kong Economic Times and The Standard in Hong Kong on 24 February 2006.

2. On 15 June 2006, the Company and GPSC entered into a Continuing Connected Transaction of Advertising Agreement. According to the respective listing rules of SSE and HKEx, the transaction constituted a connected transaction. The agreement was considered at the 23rd meeting of the Third Session of the Board held on 15 June 2006, and in respect of which, the Independent Non-executive Directors expressed their independent opinion.

For details, please refer to the announcements published in Shanghai Securities in the PRC, and Hong Kong Economic Times and The Standard in Hong Kong on 16 June 2006.

3. The Company acquired an aggregate of 9.64% shareholding in Zhong Yi Pharmaceutical jointly held by a subsidiary, Pharmaceuticals Corporation, and 33 natural persons with its own capital of RMB36,814,400. All parties entered into an equity transfer agreement on 26 July 2006. According to the respective listing rules of SSE and HKEx, the acquisition of shareholding from seven of the natural persons by the Company constituted a connected transaction. The agreement was considered at the 24th meeting of the Third Session of the Board held on 26 July 2006, and in respect of which, the Independent Non-executive Directors expressed their independent opinion. Mr. Feng Zansheng, a connected director, had abstained from voting in respect of this resolution.

For details, please refer to the announcements published in Shanghai Securities in the PRC, and Hong Kong Economic Times and The Standard in Hong Kong on 27 July 2006.

All of the above-mentioned connected transactions have been considered and passed at Board meetings of the Company, and the Independent Non-executive Directors of the Company have issued independent opinions thereon. All of the connected transactions mentioned above have complied with the relevant laws and regulations and relevant procedures have been completed.

Details of the connected transactions were set out on page 118 to 127.



## Other Events

### **(IV) MAJOR CONTRACTS AND THEIR PERFORMANCE**

During the Reporting Period, the Group did not hold on trust, sub-contract or rent assets of other companies or vice versa, which generated profit that accounted for 10% or more of the total profits for the Year.

Save as the aforementioned, the Company was not involved in other major contracts during the Reporting Period.

### **(V) DURING THE REPORTING PERIOD, THE COMPANY HAS NOT HAD ANY ENTRUSTED INVESTMENT ACTIVITIES.**

### **(VI) PERFORMANCE OF THE UNDERTAKINGS DURING THE REPORTING PERIOD**

In order to strengthen the confidence of the holders of circulating shares, and subject to relevant laws and regulations, GPL and Greatwall Corporation, being holders of shares subject to selling restrictions, has undertaken to strictly comply with the relevant requirements of "Administrative Measures for the Reform of the Segmented Share Structure of Listed Companies" and the original shares subject to selling restrictions held by GPL and Greatwall Corporation shall not be listed and traded, nor transferred within 12 months from the date of implementation of the share reform plan (being 24 April 2006). During the Reporting Period, GPL and Greatwall Corporation complied with the above undertakings (details are set out on page 11).

### **(VII) AS AT 31 DECEMBER 2006, THE CONSTRUCTION AND EQUIPMENT COMMITMENTS THAT WERE CONTRACTED BY THE GROUP BUT NOT PROVIDED FOR WAS RMB12,677,000. THE LEASE COMMITMENTS THAT WERE CONTRACTED BUT NOT PROVIDED FOR AMOUNTED TO RMB90,738,000.**

### **(VIII) DURING THE REPORTING PERIOD, THE GROUP HAS PAID AUDITOR'S REMUNERATION OF RMB988,000 AND RMB2,500,000 TO GUANGDONG YANGCHENG CERTIFIED PUBLIC ACCOUNTANTS CO., LTD., AND PRICEWATERHOUSECOOPERS RESPECTIVELY. OF THE AMOUNT PAID TO GUANGDONG YANGCHENG CERTIFIED PUBLIC ACCOUNTANTS CO., LTD., RMB880,000 WAS FOR THE 2005 ANNUAL AUDIT, AND RMB108,000 WAS FOR THE 2006 INTERIM REVIEW. AN AMOUNT OF RMB2,148,000 PAID TO PRICEWATERHOUSECOOPERS WAS FOR THE 2005 ANNUAL AUDIT AND RMB352,000 WAS FOR THE 2006 INTERIM REVIEW. BOTH THE DOMESTIC AUDITORS AND INTERNATIONAL AUDITORS HAVE PROVIDED AUDIT SERVICES TO THE COMPANY FOR 9 YEARS.**

### **(IX) DURING THE REPORTING PERIOD, NO INVESTIGATION, ADMINISTRATIVE PUNISHMENT OR PUBLIC REPRIMAND BY THE CSRC, AND NO PUNISHMENT BY HKEX WERE MADE AGAINST AND IMPOSED ON THE COMPANY, THE BOARD OR DIRECTORS.**

### **(X) THE COMPANY DID NOT HAVE ANY OTHER SIGNIFICANT EVENT DURING THE REPORTING PERIOD.**





# Other Events

## (XI) SUBSEQUENT EVENTS

1. A Share Transfer Arrangement was entered into between the Company as a transferee and GPHL, Anhui Huadong Chinese Medical Engineering Corporation Limited and five natural persons including Liu Juyan as transferors on 10 January 2007 in relation to a total of 26.04% equity interests in Guangzhou Han Fang;

On the same day, Guangzhou Han Fang and Guangzhou Huan Ye, a wholly owned subsidiary of the Company, entered into a Merger Agreement (the "Agreement"), pursuant to which both parties have agreed to the merger of Guangzhou Han Fang and Guangzhou Huan Ye through the injection of the entire business, assets and liabilities of Guangzhou Huan Ye into Guangzhou Han Fang. Guangzhou Huan Ye will be terminated whereas the enlarged Guangzhou Han Fang will continue to exist on an ongoing basis after the Merger. Pursuant to the requirements under the Listing Rules of HKEx, the Company was transferred the equity interests in Guangzhou Han Fang held by GPHL and five natural persons including Liu Juyan, and the transaction between Guangzhou Han Fang and Guangzhou Huan Ye constituted connected transactions. The Board of the Company held the 29th Meeting of the Third Session on 10 January 2007, at which the aforesaid connected transactions were considered, and the Independent Non-Executive Directors expressed their independent opinions on such connected transactions. Mr. Feng Zansheng abstained from voting in respect of the relevant resolution. Currently, the relevant procedures for approvals of the above transactions are under way.

2. On 17 January 2007, the Company agreed to purchase the Sui Kang Mansion from its subsidiary, Pharmaceuticals Corporation, at a consideration of RMB41,116,178. The relevant procedures in relation to the purchase were completed on 29 March 2007.

3. On 27 January 2007, Contract for the Transfer of Capital Contribution of Guangzhou Pharmaceuticals Corporation was entered into between Jing Xiu Tang and Pan Gao Shou, both of which are subsidiaries of the Company, and 33 natural persons and Alliance BMP Limited ("Alliance BMP"). On the same day, the Company and Alliance BMP entered into a Capital Increase Contract for Guangzhou Pharmaceuticals Corporation, JV Contract and the Articles of Association of Guangzhou Pharmaceuticals Corporation (Revised and restated). The Board of the Company held the 30th meeting of the Third Session of the Board on 26 January 2007, at which the equity transfer and capital increase (the "Event") were considered, and Mr. Feng Zansheng abstained from voting in respect of the relevant resolution.

The Event has been submitted at the First Extraordinary General Meeting of the Company in 2007 and the First Class Meeting of the Holders of Overseas-listed Foreign Shares in 2007 and the First Class Meeting of Holders of Domestic Shares in 2007 according to the standard procedures for consideration and approval, as it has resulted in a material dilution of the Company's interests in Pharmaceuticals Corporation. The Event has been approved successfully.

4. After the Reporting Period, the changes of shareholdings in all tradable shares held by the shareholders of the Company subject to selling restrictions are set as follows:

Shareholder's name	Number of shares held before change (share)	Number of shares held involved in the change (share)	Reason of the change	Number of Date of the change (share)	shares held after change
GPHL	468,603,509	(56,090,000)	—	—	412,513,509
Guangzhou Beicheng Rural Credit Cooperative	0	46,670,000	Transferred by way of court ruling	23 March 2007	46,670,000
Guangzhou Xinjiao Rural Credit Cooperative	0	4,220,000	Transferred by way of court ruling	9 February 2007	4,220,000
Guangzhou Xinfeng Rural Credit Cooperative	0	3,480,000	Transferred by way of court ruling	9 February 2007	3,480,000
Guangzhou Baiyun Rural Credit Cooperative	0	1,720,000	Transferred by way of court ruling	23 March 2007	1,720,000



# AUDITOR'S REPORT

Our reference: (2007) YC 10000  
GIICPA Ref.: 200704006968

## To all shareholders of Guangzhou Pharmaceutical Company Limited:

We have audited the Balance Sheet as at December 31, 2006, the Income Statement and the Statement of Cash Flows for the year then ended of Guangzhou Pharmaceutical Company Limited (Hereinafter refer to "the Company"), and the Consolidated Balance Sheet of the Company and its subsidiaries (Hereinafter refer to "the Group") as at December 31, 2006, the Group's Consolidated Income Statement and Consolidated Statement of Cash Flows for the year then ended, as well as the Notes to the Financial Statements.

## I. MANAGEMENT'S RESPONSIBILITY FOR THE FINANCIAL STATEMENTS

The management of the Company is responsible for the preparation of these financial statements in accordance with the Accounting Standards for Business Enterprises and the "Accounting System for Business Enterprises". These responsibilities include: designing, implementing and maintaining internal control relevant to the preparation of financial statements, so that the statements can be free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies and; making accounting estimates that are reasonable in the circumstances.

## II. AUDITOR'S RESPONSIBILITY

Our responsibility is to express an opinion on these financial statements based on our audit. We conduct our audit in accordance with Auditing Standards of Chinese CPA. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free from materials misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The selection of procedures depends on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control of the entity relevant to the preparation of the financial statements in order to design appropriate audit procedures, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies selected and the reasonableness of accounting estimates made by the management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidences we have obtained are sufficient and appropriate to provide a basis for our audit opinion.

## III. OPINION

In our opinion, the financial statements present fairly, in all material respects, the financial positions of the Company and the Group as at December 31, 2006, and the results of operations and cash flows of the Company and the Group for the year then ended in accordance with the Accounting Standards for Business Enterprises and the "Accounting System for Business Enterprises".

Guangdong Yangcheng Certified  
Public Accountants Co., Ltd.

Guangzhou, China

Chinese Certified Public Accountant  
**Wu Jiali**

Chinese Certified Public Accountant  
**Ye Weixiang**



# CONSOLIDATED BALANCE SHEET

As at 31 December 2006

Form 1-1  
In RMB Yuan

	Notes	31 December 2006	31 December 2005
<b>ASSETS:</b>			
<b>Current assets:</b>			
Monetary funds	VI— 1	489,127,579.61	616,982,949.00
Short term investments	VI— 2	—	10,902,520.00
Notes receivable	VI— 3	380,009,988.97	331,753,863.41
Dividends receivable	VI— 4	—	3,709,259.53
Interest receivable		—	—
Accounts receivable	VI— 5	1,356,441,652.87	959,776,870.53
Other receivables	VI— 6	77,295,204.75	64,432,895.76
Advances to suppliers	VI— 7	179,591,876.36	196,548,528.21
Subsidies receivable	VI— 8	4,611,755.34	3,361,927.18
Inventories	VI— 9	1,326,443,190.41	1,148,568,922.06
Prepaid expenses	VI— 10	1,190,252.35	120,665,259.48
Long-term debenture investments due within one year		—	—
Other current assets		—	—
<b>Total current Assets</b>		<b>3,814,711,500.66</b>	<b>3,456,702,995.16</b>
<b>Long-term investment:</b>			
long-term equity investment	VI— 11	75,888,816.73	70,195,741.17
long-term debenture investment		—	—
<b>Total long-term investment</b>		<b>75,888,816.73</b>	<b>70,195,741.17</b>
Including: consolidation variance	VI— 11	3,308,824.44	3,828,294.03
<b>Fixed assets</b>			
Fixed assets-cost	VI— 12	2,033,978,454.01	1,974,405,781.70
Less: Accumulated depreciation	VI— 12	742,417,277.96	658,927,334.13
Fixed assets-net value		1,291,561,176.05	1,315,478,447.57
Less: Provisions for impairment of fixed assets	VI— 12	16,991,377.83	17,902,314.55
Net of fixed assets		1,274,569,798.22	1,297,576,133.02
Construction supplies		—	—
Construction work in progress	VI— 13	123,400,529.51	159,910,405.52
Disposal of fixed assets		—	—
<b>Total fixed assets</b>		<b>1,397,970,327.73</b>	<b>1,457,486,538.54</b>
<b>Intangible assets &amp; other assets:</b>			
Intangible assets	VI— 14	111,397,998.07	98,677,683.80
Long-term prepayment	VI— 15	9,444,392.52	15,031,582.69
Other long-term assets		—	—
<b>Total intangible assets &amp; other assets</b>		<b>120,842,390.59</b>	<b>113,709,266.49</b>
<b>Deferred tax:</b>			
Deferred tax debits		—	—
<b>Total Assets</b>		<b>5,409,413,035.71</b>	<b>5,098,094,541.36</b>



# CONSOLIDATED BALANCE SHEET

As at 31 December 2005

Form 1-2  
In RMB Yuan

	Notes	31 December 2006	31 December 2005
<b>LIABILITIES &amp; SHAREHOLDERS' EQUITY</b>			
<b>Current liabilities:</b>			
Short-term borrowings	VI— 16	888,199,069.88	867,785,368.60
Notes payable	VI— 17	206,700,018.28	86,008,063.38
Accounts payable	VI— 18	861,098,479.40	869,696,059.12
Advances from customers	VI— 19	47,942,658.87	31,129,313.34
Accrued payroll		31,064,173.07	45,376,812.42
Welfare payable		44,824,740.84	52,939,978.26
Dividends payable	VI— 21	1,510,244.12	26,492.89
Taxes payable	VI— 22	36,804,038.02	24,377,413.61
Other liabilities	VI— 23	3,806,759.11	3,628,657.66
Other payables	VI— 20	248,738,381.51	191,144,199.01
Accrued expenses	VI— 24	13,393,292.08	14,220,101.58
Estimated liabilities		—	—
Long-term liabilities due within 1 year	VI— 25	—	50,000,000.00
Other current liabilities		—	—
<b>Total current liabilities</b>		<b>2,384,081,855.18</b>	<b>2,236,332,459.87</b>
<b>Long-term liabilities:</b>			
Long-term borrowings		—	—
Bonds payable		—	—
Long-term payables	VI— 26	4,694,995.54	4,716,728.21
Special payables	VI— 27	66,458,857.71	50,109,349.38
Other long-term liabilities		—	—
<b>Total long-term liabilities</b>		<b>71,153,853.25</b>	<b>54,826,077.59</b>
<b>Deferred tax:</b>			
Deferred tax credits		—	—
<b>Total liabilities</b>		<b>2,455,235,708.43</b>	<b>2,291,158,537.46</b>
<b>Minority shareholders' equity</b>			
Shareholders' equity:			
Share capital	VI— 28	810,900,000.00	810,900,000.00
Less: returned of investments		—	—
Net share capital		810,900,000.00	810,900,000.00
Capital surplus	VI— 29	1,153,220,469.96	1,149,453,755.66
Surplus reserve	VI— 30	648,062,853.70	567,243,340.17
Including: statutory public welfare fund	VI— 30	—	179,461,575.56
Retained earnings	VI— 31	175,904,623.97	93,839,656.29
Including: Cash dividend planed to allocate		68,115,600.00	56,763,000.00
Exchange difference on foreign currency statement		—	—
<b>Total shareholders' equity</b>		<b>2,788,087,947.63</b>	<b>2,621,436,752.12</b>
<b>TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY</b>		<b>5,409,413,035.71</b>	<b>5,098,094,541.36</b>



# CONSOLIDATED INCOME STATEMENT

For the year ended 31st December 2006

Form 2-1  
In RMB Yuan

Items	Notes	2006	2005
<b>I. Revenue from main operations</b>	VI—32	<b>10,241,003,505.21</b>	9,026,340,433.50
Less: Cost of main operations	VI—32	<b>8,472,227,964.38</b>	7,472,974,332.17
Sales tax and levies	VI—33	<b>25,590,982.10</b>	24,613,910.81
<b>II. Profit from main operations</b>		<b>1,743,184,558.73</b>	1,528,752,190.52
Add: Profit from other operations	VI—34	<b>41,507,991.21</b>	43,301,531.41
Less: Operating expenses		<b>752,589,938.94</b>	592,206,898.41
General and administrative expenses		<b>619,990,387.06</b>	628,434,629.66
Financial expenses	VI—35	<b>45,359,599.64</b>	43,098,471.57
<b>III. Operating profit</b>		<b>366,752,624.30</b>	308,313,722.29
Add: Investment income	VI—36	<b>7,105,537.51</b>	(8,063,080.65)
Revenue from subsidies	VI—37	<b>1,190,244.21</b>	720,456.65
Non-operating income	VI—38	<b>5,197,621.33</b>	6,194,512.31
Less: Non-operating expenses	VI—39	<b>9,883,551.10</b>	424,826.14
<b>VI. Total profit</b>		<b>370,362,476.25</b>	306,740,784.46
Less: Income tax		<b>130,826,145.19</b>	112,611,673.47
Less: Loss and gain of minority shareholders		<b>12,208,584.32</b>	9,647,562.96
Add: Unconfirmed investment profit		—	—
<b>V. Net profit</b>		<b><u>227,327,746.74</u></b>	<b><u>184,481,548.03</u></b>

## Supplemental information:

Item	2006	2005
1. Revenue from sale or disposal of department or invested company	<b>(118,223.76)</b>	4,674.88
2. Loss incurred from natural disaster	—	—
3. Total profit increased (decreased) due to accounting policy alteration	—	—
4. Total profit increased (decreased) due to accounting estimation a alteration	—	—
5. Loss from debts reconstruction	—	—
6. Others	—	—
	<b><u>—</u></b>	<b><u>—</u></b>



# SUPPLEMENTARY CONSOLIDATED INCOME STATEMENT

For the year ended 31st December 2006

Form 2-2  
In RMB Yuan

	2006				2005			
	Return on net assets (%) Fully Weighted		Earnings per share Fully Weighted		Return on net assets (%) Fully Weighted		Earnings per share Fully Weighted	
Profit for the period	diluted	average	diluted	average	diluted	average	diluted	average
Profit from main operations	62.52	64.40	2.15	2.15	58.32	60.61	1.89	1.89
Operating profit	13.15	13.55	0.45	0.45	11.76	12.22	0.38	0.38
Net profit	8.15	8.40	0.28	0.28	7.04	7.31	0.23	0.23
Net profit after deduction of extraordinary gain or loss	8.13	8.74	0.28	0.28	7.08	7.64	0.23	0.23



Annual Report 2006

# CONSOLIDATED STATEMENT OF PROFIT DISTRIBUTION

For the year ended 31st December 2006

Form 3  
In RMB Yuan

Items	2006	2005
<b>I. Net profit</b>	<b>227,327,746.74</b>	184,481,548.03
Add: Retained earnings brought forward	<b>93,839,656.29</b>	22,505,890.50
Add: Transfer from others	<b>1,886,788.57</b>	9,916,543.07
<b>II. Profit distributable</b>	<b>323,054,191.60</b>	216,903,981.60
Less: Provision of statutory surplus reserves	<b>46,889,253.85</b>	38,561,412.17
Less: Provision of statutory public welfare fund	—	28,896,962.62
Less: Provision of staff bonus and welfare fund	<b>7,680,265.53</b>	6,074,331.34
Less: Provision of reserve fund	<b>3,319,168.38</b>	2,611,460.90
Less: Provision of Enterprise expansion fund	<b>3,319,168.38</b>	2,611,460.90
Less: Profit returned to investment	—	—
<b>III. Profit distributable to shareholders</b>	<b>261,846,335.46</b>	138,148,353.67
Less: Dividend for preferred shares	—	—
Less: Provision of discretionary surplus reserves	<b>29,178,711.49</b>	24,036,197.38
Less: Dividend for ordinary shares	<b>56,763,000.00</b>	20,272,500.00
Less: Dividend for ordinary shares transfer to share capital	—	—
<b>IV. Retained earnings</b>	<b>175,904,623.97</b>	<b>93,839,656.29</b>



# CONSOLIDATED STATEMENT OF CASH FLOWS

For the year ended 31st December 2006

Form 4-1  
In RMB Yuan

Items	Notes	2006	2005
<b>I. Cash flows from operating activities</b>			
Cash received from sales of goods or rendering of services		11,523,779,844.23	10,425,844,220.73
Refund of tax and levy		12,204,580.12	12,437,554.21
Other cash received relating to operating activities	VI—40	95,244,506.32	104,674,129.82
<b>Subtotal of cash inflows</b>		<b>11,631,228,930.67</b>	<b>10,542,955,904.76</b>
Cash paid for goods or services		9,633,213,931.50	8,622,540,156.21
Cash paid to and on behalf of employees		610,918,213.58	584,881,163.05
Taxes paid		528,640,651.73	492,373,347.10
Other cash paid relating to operating activities	VI—41	819,575,700.19	696,838,662.67
<b>Subtotal of cash outflows</b>		<b>11,592,348,497.00</b>	<b>10,396,633,329.03</b>
<b>Net cash flows from operating activities</b>		<b>38,880,433.67</b>	<b>146,322,575.73</b>
<b>II. Cash flows from investing activities</b>			
Cash received from sales of investments		42,602,566.02	190,756.16
Including: cash received from sales of subsidiaries		—	—
Cash received from investment income		23,879,545.33	3,405,374.88
Net Cash received from disposal of fixed assets, intangible assets and other long-term assets		6,100,919.40	1,229,572.07
Other cash received relating to investing activities	VI—42	6,760,064.99	2,000,178.00
<b>Subtotal of cash inflows</b>		<b>79,343,095.74</b>	<b>6,825,881.11</b>
Cash paid to acquire fixed assets, intangible assets and other long-term assets		90,450,159.24	124,356,012.08
Cash paid to acquire investments		43,519,174.34	—
Including: cash paid to acquire subsidiaries		18,298,476.84	—
Other cash paid relating to investing activities	VI—43	1,341,926.31	505,373.25
<b>Subtotal of cash outflows</b>		<b>135,311,259.89</b>	<b>124,861,385.33</b>
<b>Net cash flows from investing activities</b>		<b>(55,968,164.15)</b>	<b>(118,035,504.22)</b>
<b>III. Cash flows from financing activities</b>			
Cash received from acquiring investments		—	62,626,946.09
Including: cash received from minority shareholders equity investment by subsidiaries		—	62,626,946.09
Cash received from borrowings		782,165,894.58	867,953,886.81
Other cash received relating to financing activities	VI—44	355,234,557.78	473,964,226.86
<b>Subtotal of cash inflows</b>		<b>1,137,400,452.36</b>	<b>1,404,545,059.76</b>
Cash repayments of amounts borrowed		811,165,894.58	1,075,515,518.21
Cash payments for distribution of dividends, profits or interest expenses		123,300,884.88	74,551,470.52
Including: cash payments for dividends to minority shareholders		21,747,016.72	9,835,658.26
Other cash paid relating to financing activities	VI—45	313,552,902.90	546,408,456.20
<b>Including: cash paid for minority shareholders equity of subsidiaries if decreasing share capital</b>		<b>—</b>	<b>—</b>
<b>Subtotal of cash outflows</b>		<b>1,248,019,682.36</b>	<b>1,696,475,444.93</b>
<b>Net cash flows from financing activities</b>		<b>(110,619,230.00)</b>	<b>(291,930,385.17)</b>
<b>IV. Effect of foreign exchange rate charges on cash</b>		<b>(148,408.91)</b>	<b>(198,335.24)</b>
<b>V. Net increase in cash and cash equivalents</b>		<b>(127,855,369.39)</b>	<b>(263,841,648.90)</b>





# CONSOLIDATED STATEMENT OF CASH FLOWS

For the year ended 31st December 2006

Form 4-2  
In RMB Yuan

Supplemental Information	2006	2005
<b>I. Reconciliation of net profit to cash flows from operating activities:</b>		
Net profit	227,327,746.74	184,481,548.03
Loss & gain of minority shareholders	12,208,584.32	9,647,562.96
Add: Provision for value impairment of assets	12,040,040.81	(2,734,638.44)
Depreciation of fixed assets	117,220,541.84	114,393,515.73
Amortization of intangible assets	5,783,610.45	4,648,287.25
Amortization of long-term prepaid expenses	8,095,259.81	10,699,040.96
Decrease in prepaid expenses (less: increase)	13,566,587.22	(30,829,827.49)
Increase in accrued expenses (less: decrease)	(1,403,427.07)	4,988,819.38
Losses on disposal of fixed, intangible assets and other long-term assets (less: gains)	1,520,550.06	610,373.49
Losses on scrapping of fixed assets	843,815.33	944,068.05
Financial expenses	46,933,355.26	44,443,422.11
Losses on investments (less: gains)	(7,105,537.51)	8,063,080.65
Deferred tax credit (less: debit)	—	—
Decrease in inventories (less: increase)	(180,443,359.85)	(47,282,873.71)
Decrease in operating receivables (less: increase)	(451,796,992.43)	(81,163,674.49)
Increase in operating payables (less: decrease)	234,089,658.69	(63,827,561.33)
Others	—	(10,758,567.42)
<b>Net cash flows from operating activities</b>	<b>38,880,433.67</b>	<b>146,322,575.73</b>
<b>II. Investing and financing activities that do not involve cash receipts or payments:</b>		
Conversion of debt into capital	—	—
Convertible bonds due within 1 year	—	—
Fixed assets obtained by financing lease	—	—
<b>III. Net increase in cash and cash equivalents</b>		
Cash at the end of period	489,127,579.61	616,982,949.00
Less: Cash at the beginning of the period	616,982,949.00	880,824,597.90
Add: Cash equivalents at the end of the period	—	—
Less: Cash equivalents at the beginning of period	—	—
<b>Net increase in cash and cash equivalents</b>	<b>(127,855,369.39)</b>	<b>(263,841,648.90)</b>



# STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY

For the year ended 31st December 2006

Supplementary information of Consolidated balance Sheet Part 1  
In RMB Yuan

Items	Notes	2006	2005
<b>I. Paid-in share capital:</b>	VI-28		
Beginning balance		<b>810,900,000.00</b>	810,900,000.00
Increase in the current year		—	—
Decrease in the current year		—	—
Closing balance		<b>810,900,000.00</b>	810,900,000.00
<b>II. Capital surplus:</b>	VI-29		
Beginning balance		<b>1,149,453,755.66</b>	1,126,381,425.35
Increase in the current year		<b>3,766,714.30</b>	23,072,330.31
Including: Share premium		—	—
Reserve of donated non-cash assets		<b>97,479.07</b>	440,280.48
Receipt of cash donation		—	—
Equity investment reserve		<b>16,688.40</b>	18,900,519.82
Transfer-in from government appropriation		<b>2,455,797.33</b>	1,334,850.00
Exchange difference on foreign currency capital		—	—
Other capital surplus		<b>1,196,749.50</b>	2,396,680.01
Decrease in the current year		—	—
Including: Conversion into share capital		—	—
Closing balance		<b>1,153,220,469.96</b>	1,149,453,755.66



# STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY

For the year ended 31st December 2006

Supplementary information of Consolidated balance Sheet Part 1  
In RMB Yuan

Items	Notes	2006	2005
<b>III. Statutory and discretionary surplus reserves:</b>	VI-30		
Beginning balance		<b>387,781,764.61</b>	326,870,323.86
Increase in the current year		<b>261,754,991.36</b>	67,820,531.35
Including: Amount appropriated from net income		<b>82,706,302.10</b>	67,820,531.35
Including: Statutory surplus reserve		<b>50,208,422.23</b>	41,172,873.07
Discretionary surplus reserve		<b>32,497,879.87</b>	26,647,658.28
Transferred from statutory public welfare fund		<b>179,048,689.26</b>	
Decrease in the current year		<b>1,473,902.27</b>	6,909,090.60
Including: Recovery of losses		—	—
Conversion into share capital		—	—
Distribution of cash dividend or profit		—	—
Distribution of stock dividend		—	—
Closing balance		<b>648,062,853.70</b>	387,781,764.61
Including: Statutory surplus reserve		<b>482,167,532.87</b>	253,770,252.85
<b>IV. Statutory public welfare fund:</b>	VI-30		
Beginning balance		<b>179,461,575.56</b>	153,572,065.40
Increase in the current year		—	28,896,962.62
Including: Amount appropriated from net income		—	28,896,962.62
Decrease in the current year		<b>179,461,575.56</b>	3,007,452.46
Including: Collective welfare expenditures		—	—
Closing balance		—	179,461,575.56
<b>V. Retained earnings:</b>	VI-31		
Beginning balance		<b>93,839,656.29</b>	22,505,890.50
Transferred from others		<b>1,886,788.57</b>	9,916,543.07
Net profit of the current year		<b>227,327,746.74</b>	184,481,548.03
Profit distribution of the current year		<b>147,149,567.63</b>	123,064,325.31
Closing balance		<b>175,904,623.97</b>	93,839,656.29



# STATEMENT OF PROVISION FOR IMPAIRMENT OF ASSETS

For the year ended 31st December 2006

Supplementary Information of consolidated Balance Sheet, part 2  
In RMB Yuan

Items	Beginning balance	Current increase	Current recovery		Sub-total	Closing balance
			Reversal due to recovery of assets value	Transfer-out due to other reasons		
<b>1. Total provision for bad debts</b>	57,853,581.44	18,888,408.82	2,082,648.25	7,376,646.43	9,459,294.68	67,282,695.58
Including: Accounts receivable	44,880,992.52	7,687,791.36	—	7,206,723.36	7,206,723.36	45,362,060.52
Other receivables	12,972,588.92	11,200,617.46	2,082,648.25	169,923.07	2,252,571.32	21,920,635.06
<b>2. Total provision for short-term investment</b>	8,850,080.00	—	—	8,850,080.00	8,850,080.00	—
Including: Stock investment	—	—	—	—	—	—
Debt investment	7,802,080.00	—	—	7,802,080.00	7,802,080.00	—
Fund investment	1,048,000.00	—	—	1,048,000.00	1,048,000.00	—
<b>3. Total provision for inventories</b>	1,954,226.83	2,626,803.19	—	57,711.69	57,711.69	4,523,318.33
Including: Goods in stock	1,910,664.20	1,415,663.53	—	14,149.06	14,149.06	3,312,178.67
Raw materials	43,562.63	380,461.88	—	43,562.63	43,562.63	380,461.88
<b>4. Total provision for long-term investment</b>	1,078,551.23	—	—	—	—	1,078,551.23
Including: Long-term equity investment	1,078,551.23	—	—	—	—	1,078,551.23
Long-term debt investment	—	—	—	—	—	—
<b>5. Total provision for fixed assets</b>	17,902,314.55	208,590.95	—	1,119,527.67	1,119,527.67	16,991,377.83
Including: Houses & buildings	11,643,357.48	—	—	730,258.45	730,258.45	10,913,099.03
Machinery equipment	5,581,718.63	136,990.88	—	—	—	5,718,709.51
<b>6. Provision for intangible assets</b>	966,151.46	—	—	485,451.22	485,451.22	480,700.24
Including: Patent	—	—	—	—	—	—
Trademark	—	—	—	—	—	—
<b>7. Provision for construction work in progress</b>	130,000.00	—	—	—	—	130,000.00
<b>8. Provision for loan by trust</b>	—	—	—	—	—	—
<b>9. Total</b>	<u>88,734,905.51</u>	<u>21,723,802.96</u>	<u>2,082,648.25</u>	<u>17,889,417.01</u>	<u>19,972,065.26</u>	<u>90,486,643.21</u>



# BALANCE SHEET

As at 31st December 2006

From 5-1  
In RMB Yuan

ASSETS	Notes	31 December 2006	31 December 2005
<b>Current assets:</b>			
Monetary funds		64,731,299.07	90,102,690.07
Short term investments		424,000,000.00	372,902,520.00
Notes receivable		241,335.00	—
Dividends receivable		10,000,000.00	7,720,145.68
Interest receivable		—	—
Accounts receivable	VII-1	25,967,163.20	—
Other receivables	VII-2	207,336,888.90	166,931,572.06
Advances to suppliers		5,168,611.88	—
Subsidies receivable		—	—
Inventories		9,973,596.57	—
Prepaid expenses		—	—
Long-term debenture investments due within one year		—	—
Other current assets		—	—
<b>Total current Assets</b>		<b>747,418,894.62</b>	<b>637,656,927.81</b>
<b>Long-term investment:</b>			
long-term equity investment	VII-3	2,132,494,302.74	2,025,934,634.58
long-term debenture investment		—	—
<b>Total long-term investment</b>		<b>2,132,494,302.74</b>	<b>2,025,934,634.58</b>
Including: Equity investment differences		2,050,204.88	2,351,531.83
<b>Fixed assets</b>			
Fixed assets-cost		44,496,545.75	41,236,900.52
Less: Accumulated depreciation		22,664,476.14	17,535,891.44
Fixed assets-net value		21,832,069.61	23,701,009.08
Less: Provisions for impairment of fixed assets		—	—
Net of fixed assets		21,832,069.61	23,701,009.08
Construction supplies		—	—
Construction work in progress		—	—
Disposal of fixed assets		—	—
<b>Total fixed assets</b>		<b>21,832,069.61</b>	<b>23,701,009.08</b>
<b>Intangible assets &amp; other assets:</b>			
Intangible assets		—	—
Long-term prepayment		—	912,355.01
Other long-term assets		—	—
<b>Total intangible assets &amp; other assets</b>		<b>—</b>	<b>912,355.01</b>
<b>Deferred tax:</b>			
Deferred tax debits		—	—
<b>Total Assets</b>		<b>2,901,745,266.97</b>	<b>2,688,204,926.48</b>



# BALANCE SHEET

As at 31st December 2006

From 5-2  
In RMB Yuan

LIABILITIES & SHAREHOLDERS' EQUITY	Notes	31 December 2006	31 December 2005
<b>Current liabilities:</b>			
Short-term borrowings		30,000,000.00	40,000,000.00
Notes payable		—	—
Accounts payable		22,722,272.99	—
Advances from customers		2,862,266.76	—
Accrued payroll		1,447,086.34	1,734,915.18
Welfare payable		3,606,043.16	3,487,779.14
Dividends payable		1,484,371.93	24,739.37
Taxes payable		5,941,754.21	390,052.43
Other liabilities		217,277.93	12,605.17
Other payables		7,424,011.23	5,887,062.42
Accrued expenses		2,438,473.04	2,430,164.70
Estimated liabilities		—	—
Long-term liabilities due within 1 year		—	—
Other current liabilities		—	—
<b>Total current liabilities</b>		<b>78,143,557.59</b>	<b>53,967,318.41</b>
<b>Long-term liabilities:</b>			
Long-term borrowings		—	—
Bonds payable		—	—
Long-term payables		—	—
Special payables		—	—
Other long-term liabilities		—	—
<b>Total long-term liabilities</b>		<b>—</b>	<b>—</b>
<b>Deferred tax:</b>			
Deferred tax credits		—	—
<b>Total liabilities</b>		<b>78,143,557.59</b>	<b>53,967,318.41</b>
<b>Shareholders' equity:</b>			
Share capital		810,900,000.00	810,900,000.00
Less: returned of investments		—	—
Net share capital		810,900,000.00	810,900,000.00
Capital surplus		1,152,269,928.36	1,148,510,273.74
Surplus reserve		206,325,725.05	182,088,980.38
Including: statutory public welfare fund		—	71,271,823.11
Retained earnings		654,106,055.97	492,738,353.95
Including: Cash dividend planed to allocate		68,115,600.00	56,763,000.00
<b>Total shareholders' equity</b>		<b>2,823,601,709.38</b>	<b>2,634,237,608.07</b>
<b>TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY</b>		<b>2,901,745,266.97</b>	<b>2,688,204,926.48</b>



# INCOME STATEMENT

For the year ended 31st December 2006

Form 6  
In RMB Yuan

Items	Notes	2006	2005
<b>I. Revenue from main operations</b>	VII-4	<b>306,572,500.75</b>	—
Less: Cost of main operations	VII-4	<b>292,956,150.53</b>	—
Sales tax and levies		<b>320,618.24</b>	—
<b>II. Profit from main operations</b>		<b>13,295,731.98</b>	—
Add: Profit from other operations		<b>11,326,813.05</b>	7,446,705.82
Less: Operating expenses		<b>6,513,801.61</b>	—
General and administrative expenses		<b>29,473,895.16</b>	24,099,918.37
Financial expenses		<b>(148,370.55)</b>	(1,286,468.67)
<b>III. Operating profit</b>		<b>(11,216,781.19)</b>	(15,366,743.88)
Add: Investment income	VII-5	<b>260,345,607.14</b>	201,914,521.18
Revenue from subsidies		—	—
Non-operating income		<b>14,719.86</b>	3,883.97
Less: Non-operating expenses		<b>23,790.66</b>	(6,587,090.70)
<b>VI. Total profit</b>		<b>249,119,755.15</b>	193,138,751.97
Less: Income tax		<b>6,752,308.46</b>	—
<b>V. Net profit</b>		<b>242,367,446.69</b>	193,138,751.97



# STATEMENT OF PROFIT DISTRIBUTION

For the year ended 31st December 2006

Items	Form 7 In RMB Yuan	
	2006	2005
<b>I. Net profit</b>	<b>242,367,446.69</b>	193,138,751.97
Add: Retained earnings brought forward	<b>492,738,353.95</b>	348,842,914.78
Add: Transfer from others	—	—
<b>II. Profit distributable</b>	<b>735,105,800.64</b>	541,981,666.75
Less: Provision of statutory surplus reserves	<b>24,236,744.67</b>	19,313,875.20
Less: Provision of statutory public welfare fund	—	9,656,937.60
Less: Provision of staff bonus and welfare fund	—	—
Less: Provision of reserve fund	—	—
Less: Provision of Enterprise expansion fund	—	—
Less: Profit returned to investment	—	—
<b>III. Profit distributable to shareholders</b>	<b>710,869,055.97</b>	513,010,853.95
Less: Dividend for preferred shares	—	—
Less: Provision of discretionary surplus reserves	—	—
Less: Dividend for ordinary shares	<b>56,763,000.00</b>	20,272,500.00
Less: Dividend for ordinary shares transfer to share capital	—	—
<b>IV. Retained earnings</b>	<b>654,106,055.97</b>	492,738,353.95





# STATEMENT OF CASH FLOWS

For the year ended 31st December 2006

Form 8-1  
In RMB Yuan

Items	2006	2005
<b>I. Cash flows from operating activities</b>		
Cash received from sales of goods or rendering of services	214,048,002.03	—
Refund of tax and levy	4,041.66	—
Other cash received relating to operating activities	28,436,807.31	11,308,896.03
<b>Subtotal of cash inflows</b>	<b>242,488,851.00</b>	<b>11,308,896.03</b>
Cash paid for goods or services	220,154,726.37	—
Cash paid to and on behalf of employees	12,893,468.25	6,577,370.76
Taxes paid	4,962,999.96	1,007,374.28
Other cash paid relating to operating activities	28,772,910.47	14,115,308.38
<b>Subtotal of cash outflows</b>	<b>266,784,105.05</b>	<b>21,700,053.42</b>
<b>Net cash flows from operating activities</b>	<b>(24,295,254.05)</b>	<b>(10,391,157.39)</b>
<b>II. Cash flows from investing activities</b>		
Cash received from sales of investments	40,000,000.00	—
Including: cash received from sales of subsidiaries	—	—
Cash received from investment income	152,484,561.61	115,690,821.22
Net Cash received from disposal of fixed assets, intangible assets and other long-term assets	—	250.00
Other cash received relating to investing activities	90,890,978.99	306,697,905.06
<b>Subtotal of cash inflows</b>	<b>283,375,540.60</b>	<b>422,388,976.28</b>
Cash paid to acquire fixed assets, intangible assets and other long-term assets	1,324,766.82	2,698,984.00
Cash paid to acquire investments	44,503,426.94	38,272,320.08
Including: cash paid to acquire subsidiaries	18,298,476.84	—
Other cash paid relating to investing activities	171,621,522.29	492,220,716.73
<b>Subtotal of cash outflows</b>	<b>217,449,716.05</b>	<b>533,192,020.81</b>
<b>Net cash flows from investing activities</b>	<b>65,925,824.55</b>	<b>(110,803,044.53)</b>
<b>III. Cash flows from financing activities</b>		
Cash received from acquiring investments	—	—
Cash received from borrowings	60,000,000.00	148,000,000.00
Other cash received relating to financing activities	—	51,059,940.88
<b>Subtotal of cash inflows</b>	<b>60,000,000.00</b>	<b>199,059,940.88</b>
Cash repayments of amounts borrowed	70,000,000.00	108,000,000.00
Cash payments for distribution of dividends, profits or interest expenses	56,853,552.59	21,383,911.13
Other cash paid relating to financing activities	—	59,988,928.55
<b>Subtotal of cash outflows</b>	<b>126,853,552.59</b>	<b>189,372,839.68</b>
<b>Net cash flows from financing activities</b>	<b>(66,853,552.59)</b>	<b>9,687,101.20</b>
<b>IV. Effect of foreign exchange rate charges on cash</b>	<b>(148,408.91)</b>	<b>(197,881.71)</b>
<b>V. Net increase in cash and cash equivalents</b>	<b>(25,371,391.00)</b>	<b>(111,704,982.43)</b>



# STATEMENT OF CASH FLOWS

For the year ended 31st December 2006

Form 8-2  
In RMB Yuan

Supplemental Information	2006	2005
<b>I. Reconciliation of net profit to cash flows from operating activities:</b>		
Net profit	<b>242,367,446.69</b>	193,138,751.97
Add: Provision for value impairment of assets	<b>2,213,493.94</b>	(7,109,752.25)
Depreciation of fixed assets	<b>3,435,156.49</b>	3,652,576.93
Amortization of intangible assets	—	—
Amortization of long-term prepaid expenses	<b>654,480.05</b>	580,105.42
Decrease in prepaid expenses (less: increase)	—	—
Increase in accrued expenses (less: decrease)	<b>8,308.34</b>	280,164.70
Losses on disposal of fixed, intangible assets and other long-term assets (less: gains)	<b>16,835.16</b>	—
Losses on scrapping of fixed assets	—	7,828.19
Financial expenses	<b>952,861.12</b>	1,542,864.56
Losses on investments (less: gains)	<b>(260,345,607.14)</b>	(201,914,521.18)
Deferred tax credit (less: debit)	—	—
Decrease in inventories (less: increase)	<b>(9,973,596.57)</b>	—
Decrease in operating receivables (less: increase)	<b>(21,408,161.82)</b>	846,278.53
Increase in operating payables (less: decrease)	<b>17,783,529.69</b>	(1,335,068.58)
Others	—	(80,385.68)
<b>Net cash flows from operating activities</b>	<b>(24,295,254.05)</b>	(10,391,157.39)
<b>II. Investing and financing activities that do not involve cash receipts or payments:</b>		
Conversion of debt into capital	—	—
Convertible bonds due within 1 year	—	—
Fixed assets obtained by financing lease	—	—
	—	—
<b>III. Net increase in cash and cash equivalents</b>		
Cash at the end of period	<b>64,731,299.07</b>	90,102,690.07
Less: Cash at the beginning of the period	<b>90,102,690.07</b>	201,807,672.50
Add: Cash equivalents at the end of the period	—	—
Less: Cash equivalents at the beginning of period	—	—
<b>Net increase in cash and cash equivalents</b>	<b>(25,371,391.00)</b>	(111,704,982.43)



Annual Report 2006

# NOTES TO THE FINANCIAL STATEMENTS

## I. BASIC CONDITION OF THE COMPANY

Guangzhou Pharmaceutical Company Limited (the "Company") is a joint stock company with limited liability established initially in this form in the People's Republic of China pursuant to a reorganization of eight Chinese patent medicine manufacturing entities and three pharmaceutical trading entities formerly under the supervision and control of Guangzhou Pharmaceutical Holdings Limited (the "Holding") with the capital injection of the state owned equity relating to the operating assets in accordance with the TGS [1997] 139 article issued by the Economic Structure Reform Committee of the State. The Company obtained an enterprise legal person business license with the official code of 4401011101830 on September 1, 1997.

Pursuant to the document with ref. TGS [1997] 145 issued by the Economic Structure Reform Committee of the State and the ZWF [1997] 56 article issued by the Securities Committee of the State Council, the Company issued 219.9 million H shares of stock listed on the Stock Exchange of Hong Kong Limited in October 1997. Approved by the China Securities Regulatory Committee, the Company issued 78 million A shares on January 10, 2001.

In April 2006, the Company has implemented share discription reformation that has been completed within the current month. Following the reformation, the total shares of the Company are 810,900,000, among which 468,603,509 shares are state shares held by the Holding, taking 57.79%; 20,996,491 shares are state shares held by China Great Wall Asset Management Corporation, taking 2.59%; 321,300,000 shares are public shares, taking 39.62%.

The Company and its consolidated subsidiaries (the "Group") engage in capital management, investment, development, financing, the development and manufacturing of Chinese patent medicine, the manufacturing of biological products, health protection medicines and drinks, and the wholesale, retail and import & export of Chinese patent medicine, western pharmaceutical products and various medical apparatus.

The Group's current structure includes eight Chinese patent medicine manufacturing entities, one chemical materials medicine manufacturing entity, two medical research & development entities and four pharmaceutical trading entities.

## II. PRINCIPAL ACCOUNTING POLICIES, ACCOUNTING ESTIMATES AND METHOD FOR PREPARATION OF CONSOLIDATED FINANCIAL STATEMENTS

### 1. Accounting System

The Group implements the Accounting Standards for Business Enterprises and the Accounting System for Business Enterprises and the supplementary stipulations.

### 2. Accounting Year

Accounting year of the Group coincides with the calendar year, i.e., from January 1 to December 31 on the Gregorian calendar.

### 3. Bookkeeping Currency

The Group uses Renminbi ("RMB") as its bookkeeping currency.

### 4. Basis of Recording and Valuation

The Group adopts accrual concept as basis of recording and historical cost as basis of valuation.

### 5. Foreign Currency Translation

Foreign currency transactions during the year are translated into RMB at the exchange rates (middle price) prevailing at the transaction dates. Monetary assets and liabilities denominated in foreign currencies at the balance sheet date are translated into RMB at the exchange rates (middle price) prevailing at the balance sheet date. The amount of exchange differences arising from the special borrowings denominated in foreign currency at the end of year should be capitalized in the specific period before the fixed assets being acquired or constructed has reached its expected usable condition and should be charged as cost of construction work in progress; the amount of exchange differences arising from other accounts denominated in foreign currency should be charged as financial expenses. Exchange differences arising from these translations are recorded as financial expenses of the current period.



# NOTES TO THE FINANCIAL STATEMENTS

## II. PRINCIPAL ACCOUNTING POLICIES, ACCOUNTING ESTIMATES AND METHOD FOR PREPARATION OF CONSOLIDATED FINANCIAL STATEMENTS *(Continued)*

### 6. Cash Equivalents

Cash equivalents are defined as investments that are short-term, highly liquid, readily convertible to cash of known amount and are subject to a low risk of change in value at the time the Group prepares the statement of cash flows.

### 7. Short-term Investments

#### (1). Valuation Method on Acquisition

Short-term investments are recorded at total price on acquisition (deducting the cash dividends or interest that have been declared but not received) and related levies. The amount of a short-term investment acquired from debt restructuring should be determined at the book value of the receivables; while the amount of a short-term investment received through non-monetary transactions should be determined according to the book value of the assets transferred out.

#### (2). Accrual of Provision for Short-term Investments Write-down

At the end of the mid-year and the year, short-term investment write-down should be accrued or adjusted at the difference between the lower cost and the market price.

#### (3). Recognition of Proceeds on Short-term Investment

Proceeds on short-term investment should be recognized upon disposal of short-term investments. Cash dividends or interest distributed during the holding period will be offset against the cost of investments or related receivables.

### 8. Accounting for Bad Debts

#### (1). Standards for Bad Debt Recognition:

- A. If the debtor becomes bankrupt or dies, the amount remaining after repayment by liquidation property or legacy, will be the bad debts.
- B. If the debtor does not make repayment for over three years and there is obvious evidence showing that the receivables can not be recalled, the amount remaining will be bad debts upon the approval of the board of directors.

#### (2). Accounting for Bad Debt Losses

The Group makes provision for bad debts. The provision will be reversed when bad debts arise.

#### (3). Accrual Method and Proportion of Bad Debt Provision

- A. According to the accrual standards of provision for bad debts approved by the board of directors, the Group adopts aging analysis method for accrual of bad debt provisions. In addition, the Group makes special provision for high-risk receivables in light of the financial status and solvency of the debtor.

The accrual rates are based on the aging of receivable balances as follows:

<b>Aging of Receivables</b>	<b>Accrual Rate (%)</b>
Within 1 year	1
1~2 years	10
2~3 years	30
3~4 years	50
4~5 years	80
Over 5 years	100

- B. The abovementioned receivables include accounts receivable and other receivables. The Group makes provisions for other receivables after deduction of the balance of related party debtors, unreimbursed business expenditures and other current accounts irrelevant to repayment of accounts.



# NOTES TO THE FINANCIAL STATEMENTS

## II. PRINCIPAL ACCOUNTING POLICIES, ACCOUNTING ESTIMATES AND METHOD FOR PREPARATION OF CONSOLIDATED FINANCIAL STATEMENTS *(Continued)*

### 9. Inventories

(1). Classification of Inventories

Inventories of the Group include finished goods, goods in stock, work-in-process, raw materials of various kinds, materials in transit, low-value consumables and packaging materials, etc.

(2). Inventory System

The Group adopts perpetual inventory system.

(3). Valuation Method on Acquisition and Dispatch

Consolidated subsidiaries include manufacturing enterprises and commercial enterprises. The respective basis of valuation is as follows:

A. Manufacturing enterprises:

If raw materials and finished products are stated at planned cost, inventories are recorded at planned cost upon daily receipt and dispatch. At the end of each month, the amount of inventories stated at planned cost will be adjusted for price variances borne by them to arrive at the actual cost; if stated at actual cost, inventories are accounted for on a weighted average basis or first-in-first-out basis.

B. Commercial enterprises:

Inventories of wholesale enterprises are stated at acquisition cost on first-in-first-out basis.

Inventories of retail enterprises are stated using the selling price method. The amount is adjusted for price variances at month-end.

The amount of inventories acquired from debt restructuring should be determined at the book value of the receivables; while the amount of inventories received through non-monetary transactions should be determined according to the book value of the assets transferred out.

(4). Amortization of Low-value Consumables and Packaging Materials

Low-value consumables and packaging materials are recorded at actual cost and amortized in full amount upon application.

(5). Accrual Method of Provision for Inventory Write-down

The Group examines the inventories at the end of each period. Where the cost of inventories is higher than the recoverable amount because the inventories are damaged, completely or partially obsolescent, or the selling price is lower than the cost, provision for inventory write-down should be made on the difference between the cost and the lower recoverable amount.

The recoverable amount refers to the amount of an estimated selling price after deducting the estimated completion cost and estimated necessary selling expenses during the ordinary activities of the Group.



# NOTES TO THE FINANCIAL STATEMENTS

## II. PRINCIPAL ACCOUNTING POLICIES, ACCOUNTING ESTIMATES AND METHOD FOR PREPARATION OF CONSOLIDATED FINANCIAL STATEMENTS *(Continued)*

### 10. Long-term Investments

(1). Valuation Method on Acquisition

Long-term investments should be recorded at the initial cost on acquisition, which includes related taxes and commission fees etc.. The amount of equity investments acquired from debt restructuring should be determined at the book value of the receivables; while the amount of equity investments received through non-monetary transactions should be determined according to the book value of the assets transferred out.

(2). Long-term Equity Investments

The cost method is applied for long-term equity investments when an investor does not have control, joint control or significant influence over the investee; the equity method is applied for long-term equity investments when an investor can control, jointly control or has significant influence over the investee.

When the equity method is adopted, differences between the higher initial cost and the investor's share of net assets of the investee are amortized evenly over the investment period, if any, as stipulated in the investment contract. If the investment period is not specified in the contract, the said difference is amortized over a period no more than 10 years. The shortfall of the investment cost over the investor's share of net assets of the investee is recorded as capital surplus (reserve of equity investment). The credit balance of equity investment differences incurred before the effective date of the document ref. CK[2004] 3 should be amortized according to the original regulations; those incurred in the re-investment should be treated according to the document ref. CK[2004] 3.

(3). Long-term Debenture Investments

Long-term debenture investments of the Group are stated at actual cost and investment income is accounted for at cost method.

Premium or discount is amortized at a straight-line method when recognizing related interest income over the period between the acquisition date and the maturity date of the debenture.

(4). Provision for Impairment of Long-term Investments

At the end of the mid-year and the year, approved by the board of directors, if the carrying amount of a long-term investment is lower than its recoverable amount as a result of continuous decline in market value or deterioration in operating conditions of the investment, and the decline will not be recovered in the foreseeable future, the Group will make the provision for this based on the difference between the lower recoverable amount and the carrying amount of the long-term investment. Since 2004, when accruing provision for impairment of long-term investments, equity investment differences incurred in the previous years should be treated according to the document ref. CK [2004] 3.

Provision for impairment of long-term equity investments should be determined specially on each investment item.



# NOTES TO THE FINANCIAL STATEMENTS

## II. PRINCIPAL ACCOUNTING POLICIES, ACCOUNTING ESTIMATES AND METHOD FOR PREPARATION OF CONSOLIDATED FINANCIAL STATEMENTS *(Continued)*

### 11. Entrust Loan

The loan lent out through financial organs by entrustment is accounted for at the actual entrusted amount lent out. Interest receivable from such loan is accrued at the rate regulated in the entrust loan contract at the end of each year. Accrual of interest on entrust loan should be ceased when the interest due cannot be recovered and interest accrued should be written off concurrently.

At the end of the mid-year and the year, the Group will check the principal of the entrust loan thoroughly. Where the principal is higher than the recoverable amount, the difference is recognized as a provision for impairment.

### 12. Valuation and Depreciation Method of Fixed Assets

#### (1). Standards of Fixed Assets

Fixed assets include houses and buildings, machinery equipment, vehicles, and tools etc. with useful lives over one year and unit cost more than RMB2, 000.

#### (2). Valuation of Fixed Assets upon Acquisition

Fixed assets are stated at actual cost.

The amount of fixed assets acquired from debt restructuring should be determined at the book value of the receivables; while the amount of fixed assets received through non-monetary transactions should be determined according to the book value of the assets transferred out.

#### (3). Accrual Method of Fixed Assets Depreciation

Fixed assets are depreciated over their useful lives at straight-line method. Depreciation rates are determined based on the category, estimated useful lives and estimated rate of net residual value of fixed assets.

Renovation expenses of fixed assets to be capitalized are depreciated separately over the shorter of the interim period between the two renovation projects or the remaining usable year at straight-line method. Improvement expenditures of fixed assets under operational lease are depreciated separately over the shorter of the remaining lease term or the remaining usable year at straight-line method.

Fixed assets category	Useful lives	Annual Depreciation rate (%)
Houses and buildings	15~50 years	1.80~6.60
Machinery equipment	4~18 years	5~24.75
Vehicles	5~10 years	9~19.80
Electric equipment	5~10 years	9~19.80
Office equipment	4~8 years	11.25~24.75
Renovation of fixed assets	5 years	20

If provision for impairment of fixed assets has been provided in a full amount, no depreciation shall be made any more.

For fixed assets accrued with provision for impairment, depreciation rate and depreciation amount should be recomputed at the book amount of fixed assets and their useful years; if the value of fixed assets with provision for impairment is recovered, depreciation rate and depreciation amount should be recomputed at the book amount of fixed assets after recovery and their useful years.





# NOTES TO THE FINANCIAL STATEMENTS

## II. PRINCIPAL ACCOUNTING POLICIES, ACCOUNTING ESTIMATES AND METHOD FOR PREPARATION OF CONSOLIDATED FINANCIAL STATEMENTS *(Continued)*

### 12. Valuation and Depreciation Method of Fixed Assets *(continued)*

#### (4). Accrual of Provision for Impairment of Fixed Assets

The Group checks the fixed assets item by item at the end of the mid-year and the year. If the recoverable amount is lower than the carrying amount due to continuing decline in market value, technical obsolescence, physical damage or long idleness, the Group should make provision for impairment at their difference on a single item basis.

### 13. Construction Work in Progress

#### (1). Valuation Method on Acquisition

Project cost of construction work in progress is valued at actual cost and transferred to fixed assets when the work reaches its expected usable condition. If the final cost of construction has not been ascertained, the fixed assets should be recorded at an estimated amount and adjusted according to the cost actually incurred after the final cost of construction has been ascertained.

#### (2). Accrual of Provision for Impairment of Construction Work in Progress

In the case that the construction work is suspended for a long period and will not restart in the foreseeable future, or is outdated in function or technology, and the economic benefit flowed to the entities is very uncertain, provision will be made for the difference between the carrying amount and the lower recoverable amount on a single item basis at the end of the mid-year and the year.

### 14. Intangible Assets

#### (1). Valuation Method on Acquisition

Intangible assets of the Group are recorded at actual cost.

The amount of intangible assets acquired from debt restructuring should be determined at the book value of the receivables; while the amount of intangible assets received through non-monetary transactions should be determined according to the book value of the assets transferred out.

#### (2). Amortization Method

Intangible assets are amortized at straight-line method. If either the relevant contract or the laws stipulates the beneficial period or the effective period, an intangible asset should be amortized evenly over the years no more than the stipulated period; if both the relevant contract and the laws stipulate the said period, an intangible asset should be amortized evenly over the shorter one; if neither the relevant contract nor the laws stipulates the said period, an intangible asset should be amortized evenly over no more than 10 years.

#### (3). Accrual of Provision for Impairment of Intangible Assets

At the end of the mid-year and the year, if the intangible asset's capacity to create economic benefit has been adversely affected or its value is not likely to be recovered as a result of being replaced by a new technology and its market value declines drastically, provision will be made for the difference between the carrying amount and the lower recoverable amount on a single item basis.





# NOTES TO THE FINANCIAL STATEMENTS

## II. PRINCIPAL ACCOUNTING POLICIES, ACCOUNTING ESTIMATES AND METHOD FOR PREPARATION OF CONSOLIDATED FINANCIAL STATEMENTS *(Continued)*

### 15. Long-term Prepayments

Long-term prepayments are stated at actual cost and amortized evenly over the anticipated beneficial period.

Organization expenses are recorded as long-term prepayments when they are incurred, and charged in lump sum as losses of the month commencing operation.

### 16. Accounting Treatment for Borrowing Costs

#### (1). Recognition of Borrowing Costs Capitalization

Ancillary expenses incurred in connection with the special borrowings should be capitalized before the fixed asset being acquired or constructed has reached its expected usable condition. If the ancillary expenses are small in amount, they may be recorded as gains or losses of the current period.

Interest incurred, discounts or premiums to be amortized, and the exchange differences which arising from special borrowings in connection with the acquisition and construction of a fixed asset should be capitalized when the following three conditions are synchronously satisfied: expenditures for the asset are being incurred; borrowing costs are being incurred; acquisition and construction activities that are necessary to prepare the asset for its expected usable condition have been commenced.

Capitalization of borrowing costs should be suspended if the acquisition or construction of a fixed asset is interrupted abnormally and lasts continuously for and more than 3 months; or after the fixed asset being acquired or constructed has reached its expected usable condition.

If part of a fixed asset being acquired or constructed has been completed respectively and put into use individually, capitalization of such part of borrowing costs should be suspended.

Borrowing costs incurred in connection with ordinary borrowings or special borrowings that do not meet the capitalization requirements should be recorded as current gains or losses upon occurrence.

#### (2). Capitalization Term of Borrowing Costs

The capitalization amount should be accounted for on a quarterly basis.

#### (3). Capitalization Amount of Borrowing Costs Incurred in Connection with Special Borrowings

Capitalization amount of interest for each accounting period = weighted average amount of accumulated expenditures incurred for the acquisition or construction of a fixed asset up to the end of the current year \* weighted average interest rate of the loan

Eligible ancillary expenses and exchange differences are to be capitalized directly at the actual amount occurred.



# NOTES TO THE FINANCIAL STATEMENTS

## II. PRINCIPAL ACCOUNTING POLICIES, ACCOUNTING ESTIMATES AND METHOD FOR PREPARATION OF CONSOLIDATED FINANCIAL STATEMENTS *(Continued)*

### 17. Recognition of Revenue

- (1). Revenue from sales of goods

Revenue from sales of goods is recognized when the major risks and rewards of the title to the goods are passed to customers and the Group does not execute the continuing right of supervision and actual control over the goods, economic benefit relevant to the transaction can be flowed into the enterprise and, relating revenue and cost of goods sold can be measured reliably.

- (2). Revenue from rendering services

When the service is started and completed within the same accounting year, revenue should be recognized at the time of completion of the service as well as receiving the payment or payment evidences. If the service is started and completed in different accounting years and the outcome of the transaction involving the rendering of services can be estimated reliably, revenue should be recognized at the balance sheet date by the use of the percentage of completion method.

- (3). Revenue from releasing use right of assets

Revenue from releasing use right of assets shall be recognized according to the contract or agreement when the economic benefit associated with the transaction can be flowed into the enterprise and the amount of revenue can be measured reliably.

### 18. Accounting Treatment for Income Tax

The Group accounts for income tax using the tax payable method.

### 19. Basis of Preparation of the Consolidated Financial Statements

- (1). The consolidated financial statements are prepared in accordance with the article "Temporary Regulation on Consolidated Financial Statements" and relevant documents based on the individual financial statements and other information of the Company and its consolidated subsidiaries. However, as regulated in the CKEZ [1996] 2 article "Reply to the Quaere on the Consolidation Scope for the Consolidated Financial Statements" issued by the Ministry of Finance, subsidiaries in special industry or in small scale are not in the consolidation scope. When consolidating the financial statements, the following items are eliminated: internal equity investment and owners' equity of subsidiaries, proceeds on internal investments and profit distribution of subsidiaries, internal transactions, internal debts and claim; and adjustments are made on consolidated surplus reserve. Joint ventures that are in the consolidation scope are consolidated at the proportional consolidation method when preparing the consolidated financial statements.
- (2). There are no significant differences between the accounting policies and the accounting treatments adopted by the Company and its subsidiaries.



# NOTES TO THE FINANCIAL STATEMENTS

## III. TAXATION

### 1. Circulating taxes and surcharges

(1). Circulating taxes

Taxable items	Tax	Rate (%)
Revenue from sales of goods	Value-added tax	17
Revenue from transfer of materials	Value-added tax	17
Revenue from rendering services	Business tax	5
Revenue of rentals	Business tax	5
Revenue from financial lending	Business tax	5
Revenue from sales of wine products	Consumption tax	10

(2). Urban Maintenance and construction tax

It is calculated and paid based on 7% of the total amount of the circulating tax. Subsidiaries of the Group that are foreign invested enterprises are exempted from urban maintenance and construction tax in accordance with PRC regulations.

(3). Education surcharge

It is calculated and paid based on 3% of the total amount of the circulating tax. Subsidiaries of the Group that are foreign invested enterprises are exempted from education surcharge in accordance with PRC regulations.

### 2. Enterprise income tax

The Group pays enterprise income tax at the rate of 33% in accordance with the Temporary Regulation of Enterprise Income Tax of PRC.

Pursuant to the stipulations of the Income Tax Law of PRC for Enterprises with Foreign Investment and Foreign Enterprises, Guangzhou Qixing Pharmaceutical Co., Ltd., a subsidiary of the Group, pays the enterprise income tax at the rate of 24% and local income tax rate of 3%. Guangzhou Wanglaoji Pharmaceutical Co., Ltd., joint venture of the Group, pays the enterprise income tax at the rate of 24% and local income tax rate of 3% and, since March 2005, enjoys the preferential tax policy, i.e., from the year beginning to make profit, it is exempted from enterprise income tax and local income tax in the first and second years and allowed a fifty percent reduction from the third to the fifth years. The current year is the second year that Guangzhou Wanglaoji Pharmaceutical Co., Ltd. can be exempted from the enterprise income tax and the local income tax.



# NOTES TO THE FINANCIAL STATEMENTS

## IV. SUBSIDIARIES AND JOINT VENTURES

### (1). All subsidiaries, joint ventures controlled by the Company and the consolidation scope (Monetary unit: RMB'000)

Name of the investee	Business	Paid-in Capital/ Share Capital	Actual Investment of the Group	% of Equity Interest	Consolidated or not	Remark
Guangzhou Hanfang Modern Chinese Patent Medicine Research & Development Co., Ltd.	Research & development of medicine and products of health care	127,760	93,330	72.96	Yes	
Guangzhou Baidi Biotechnology Co., Ltd.	Research & development of medicine	83,600	80,000	95.69	Yes	
Guangzhou Huanye Pharmaceutical Co., Ltd.	Manufacturing chemical materials for medicine	6,000	6,000	100	Yes	remark 1
Guangzhou Xingqun Pharmaceutical Co., Ltd.	Production of Chinese patent medicine	77,170	68,670	88.99	Yes	
Guangzhou Zhongyi Pharmaceutical Co., Ltd.	Production of Chinese patent medicine	166,000	166,000	100	Yes	remark 2
Guangzhou Chenlijij Pharmaceutical Factory	Production of Chinese patent medicine	112,850	112,850	100	Yes	
Guangzhou Qixing Pharmaceutical Factory	Production of Chinese patent medicine	82,420	82,420	100	Yes	
Guangzhou Jing Xiu Tang Pharmaceutical Co., Ltd.	Production of Chinese patent medicine	86,230	76,230	88.4	Yes	
Guangzhou Pangaoshou Pharmaceutical Co., Ltd.	Production of Chinese patent medicine	65,440	57,440	87.77	Yes	
Guangzhou Wanglaoji Pharmaceutical Co., Ltd.	Production of Chinese patent medicine	204,760	98,380	48.0465	Yes	Proportional consolidation
Guangzhou Pharmaceuticals Corporation	Sales of western pharmaceutical products and medical apparatus	222,000	215,330	96.9941	Yes	
Guangzhou Chinese Medicine Corporation	Sales of Chinese patent medicine and Chinese medical materials	75,030	75,030	100	Yes	
Guangzhou Pharmaceutical Import & Export Corporation	Import and export of medicine	15,000	15,600	100	Yes	
Guangzhou Pharmaceutical Ying Bang Trading Co., Ltd.	Trading of Chinese patent medicine and Chinese medical material	18,410	3,890	51	Yes	
Guangxi Ying Kang Pharmaceutical Co., Ltd.	Production of Chinese patent medicine	31,880	21,720	51	Yes	

Remark 1: In the reporting period, the Group has purchased the shares of Guangzhou Huanye Pharmaceutical Co., Ltd. Formerly held by the natural persons. From this reporting period, the holding proportion of the Group in this company is increased from 59.7% to 100%.

Remark 2: In the reporting period, the Group has purchased the shares of Guangzhou Zhongyi Pharmaceutical Co., Ltd. Formerly held by the natural persons. From this reporting period, the holding proportion of the Group in this company is increased from 97.016% to 100%.



# NOTES TO THE FINANCIAL STATEMENTS

## IV. SUBSIDIARIES AND JOINT VENTURES *(Continued)*

### (2). Subsidiaries and joint ventures not included in the consolidation scope

The Group holds 51% of equity interest in Guangzhou Jing Xiu Tang 1790 Trading Co., Ltd., 50% of Guangzhou Lianjie Computer Technology Co., Ltd. and 46.10% of Guangzhou Pharmaceutical Football Club Co., Ltd.. As the shares on the total of assets, sales revenue and net profit of the three companies are under 10% of the total of assets, sales revenue, and net profit of the Group, they are not included in the consolidation in accordance with the Reply to the Quære on the Consolidation Scope for the Consolidated Financial Statements with reference No. CKEZ [1996] 2 and the principle of materiality.

### (3). Companies consolidated under proportional consolidation method

Shares' proportion of Guangzhou Wanglaoji Pharmaceutical Co., Ltd. held by Hong Kong Tongxing Pharmaceutical Co., Ltd. and the Group are both 48.0465%. Thus, the company is consolidated into the Group by adopting the proportional consolidation method.

## V. PROFIT DISTRIBUTION

The profit after tax will be distributed in the following sequence:

- 1). Making up losses;
- 2). Allocation to statutory surplus reserve fund;
- 3). Allocation to discretionary surplus reserve fund;
- 4). Payment of dividends.

The distribution of profit after tax and payment of dividends will be proposed by the board of directors and approved by the shareholders' general meeting. Unless the shareholders come to other resolution, the board of directors can be authorized by the shareholders' general meeting to declare and pay interim dividends.

## VI. NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (ALL AMOUNTS ARE STATED IN RMB YUAN UNLESS OTHERWISE STATED)

### 1. Monetary funds

	Closing Balance	Beginning Balance
Cash in hand	1,166,253.91	1,304,902.35
Cash in bank	477,346,558.17	610,639,962.83
Other monetary funds	10,614,767.53	5,038,083.82
	<u>489,127,579.61</u>	<u>616,982,949.00</u>

#### 1) Breakdown of cash in bank

	Closing Balance	Beginning Balance
Current RMB deposit	403,845,521.05	512,242,421.39
Current USD deposit	5,605,116.87	2,275,702.93
Current HKD deposit	14,083,840.25	10,728,776.51
Time deposit	53,812,080.00	85,393,062.00
	<u>477,346,558.17</u>	<u>610,639,962.83</u>



# NOTES TO THE FINANCIAL STATEMENTS

## VI. NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (ALL AMOUNTS ARE STATED IN RMB YUAN UNLESS OTHERWISE STATED) (Continued)

### 1. Monetary funds (continued)

#### 2) Breakdown of other monetary funds

	Closing Balance	Beginning Balance
Out-port bank deposit	50,772.22	51,602.35
Credit card deposit	212,621.90	538,487.09
L/C guaranty deposit	975,820.03	1,458,961.42
Bank bill deposit	7,950,000.00	—
Others	1,425,553.38	2,989,032.96
	<u>10,614,767.53</u>	<u>5,038,083.82</u>

At the end of the year, the Group holds deposit of HKD 7,111 thousand (equivalent to RMB 7,145 thousand) and USD 0.9 thousand (equivalent to RMB 7 thousand) in Hong Kong.

### 2. Short-term investments and provision for short-term investment write-down

	Closing Balance		Beginning Balance	
	Amount	Write-down Provision	Amount	Write-down Provision
Bond investment	—	—	9,752,600.00	7,802,080.00
Including: Treasury bond	—	—	9,752,600.00	7,802,080.00
Fund Investment	—	—	10,000,000.00	1,048,000.00
	<u>—</u>	<u>—</u>	<u>19,752,600.00</u>	<u>8,850,080.00</u>

The closing balance of short-term investment decreases by 19,753 thousand, representing 100% as compared with the beginning balance, mainly because the Group has sold the Golden Eagle Fund in this reporting period and reversed the accrued write-down provision accordingly; the Group has transferred the treasury bonds under trusteeship of Nanfang Security Co., Ltd. to Other Receivables and transferred the accrued write-down provision accordingly.

### 3. Notes receivable

Category of the Notes	Closing Balance	Beginning Balance
Bank acceptance bill	151,089,303.86	207,972,477.00
Trade acceptance bill	228,920,685.11	123,781,386.41
	<u>380,009,988.97</u>	<u>331,753,863.41</u>

At the end of the reporting period, the amount of the trade acceptance bill discounted but undue is 139,613 thousand.

At the end of the reporting period, the amount of the bank acceptance bill discounted but undue is 61,738 thousand.

### 4. Dividends receivable

	Closing Balance	Beginning Balance
Dividends receivable from Guangzhou Wanglaoji Pharmaceutical Co., Ltd.	<u>—</u>	<u>3,709,259.53</u>

The closing balance of dividends receivable decreases by 3,709 thousand, representing 100% as compared with the beginning balance for the reason that the dividends for the year 2005 of Guangzhou Wanglaoji Pharmaceutical Co., Ltd. was received in the current reporting period.



# NOTES TO THE FINANCIAL STATEMENTS

## VI. NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (ALL AMOUNTS ARE STATED IN RMB YUAN UNLESS OTHERWISE STATED) (Continued)

### 5. Accounts receivable

- 1) Aging analysis of accounts receivable as of December 31, 2006:

Aging	Closing Balance			
	Amount	% of the Total	Accrual Proportion of Bad Debt Provision	Bad Debt Provision
Within 1 year	1,358,046,781.98	96.88%	1.02%	13,897,032.64
1 — 2 years	9,285,500.33	0.66%	20.25%	1,880,023.03
2 — 3 years	7,590,804.55	0.54%	45.09%	3,422,759.26
3 — 4 years	4,010,045.58	0.29%	88.33%	3,542,239.97
4 — 5 years	9,701,958.37	0.69%	97.41%	9,451,383.04
Over 5 years	13,168,622.58	0.94%	100.00%	13,168,622.58
	<u>1,401,803,713.39</u>	<u>100.00%</u>		<u>45,362,060.52</u>

Aging	Beginning Balance			
	Amount	% of the Total	Accrual Proportion of Bad Debt Provision	Bad Debt Provision
Within 1 year	946,271,187.05	94.19%	1.00%	9,120,741.30
1 — 2 years	18,585,749.53	1.85%	12.53%	2,328,004.52
2 — 3 years	7,747,640.01	0.77%	42.81%	3,317,116.23
3 — 4 years	11,859,603.02	1.18%	88.04%	10,441,462.88
4 — 5 years	3,182,169.21	0.32%	83.66%	2,662,153.36
Over 5 years	17,011,514.23	1.69%	100.00%	17,011,514.23
	<u>1,004,657,863.05</u>	<u>100.00%</u>		<u>44,880,992.52</u>

From the aforementioned closing balance, no account is due from shareholders with 5% or more voting shares.

- 2) At the end of the year, 104,636 thousand is owed by the top five customers with largest amount, representing 7.46% of the total balance.
- 3) Compared with the beginning balance, the closing balance increases by 397,146 thousand, representing 39.53%, for the reason that in the current year, sale grows continuously as the Group keeps expanding its market and prolongs credit term of certain customers for higher market share.
- 4) The current 129 reversals of accounts receivable amounted to 7,207 thousand without any related party transactions.



# NOTES TO THE FINANCIAL STATEMENTS

## VI. NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (ALL AMOUNTS ARE STATED IN RMB YUAN UNLESS OTHERWISE STATED) (Continued)

### 6. Other receivables

- 1) Aging analysis of other receivables as of December 31, 2006:

Aging	Closing Balance			
	Amount	% of the Total	Accrual Proportion of Bad Debt Provision	Bad Debt Provision
Within 1 year	64,692,862.88	65.20%	5.37%	354,547.67
1 — 2 years	1,429,628.48	1.44%	6.91%	98,738.36
2 — 3 years	1,485,899.90	1.50%	7.96%	118,241.86
3 — 4 years	17,549,037.59	17.69%	60.69%	10,651,318.11
4 — 5 years	4,391,539.03	4.43%	81.44%	3,576,633.54
Over 5 years	9,666,871.93	9.74%	73.67%	7,121,155.52
	<u>99,215,839.81</u>	<u>100.00%</u>		<u>21,920,635.06</u>

Aging	Beginning Balance			
	Amount	% of the Total	Accrual Proportion of Bad Debt Provision	Bad Debt Provision
Within 1 year	15,761,916.68	20.36%	1.91%	300,612.12
1 — 2 years	18,015,695.32	23.27%	0.88%	159,151.77
2 — 3 years	16,811,537.47	21.72%	16.84%	2,830,830.91
3 — 4 years	5,337,371.51	6.90%	24.20%	1,291,900.00
4 — 5 years	9,783,921.53	12.64%	12.68%	1,240,695.60
Over 5 years	11,695,042.17	15.11%	61.13%	7,149,398.52
	<u>77,405,484.68</u>	<u>100.00%</u>		<u>12,972,588.92</u>

- 2). In the closing balance of other receivables, the amount dues from shareholder with 5% or more voting shares is that dues from the Holding with an amount of 4,071 thousand.
- 3). The five largest amounts of other receivables add up to 23,288 thousand, accounting for 23.47% of the total.
- 4). The closing balance of bad debt provision for other receivables increases by 8,948 thousand, representing 68.98% as compared with the beginning balance. The reason is that as the treasury bond under trusteeship of Nanfang Security Co., Ltd. has been transferred to other receivables, the accrued provision for write-down with the amount of 7,802 thousand has been transferred to bad debt provision accordingly.





# NOTES TO THE FINANCIAL STATEMENTS

## VI. NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (ALL AMOUNTS ARE STATED IN RMB YUAN UNLESS OTHERWISE STATED) (Continued)

### 7. Advances to suppliers

	Closing Balance	Beginning Balance
Advances to suppliers	<u>179,591,876.36</u>	<u>196,548,528.21</u>

- From the aforementioned closing balance, no account is advanced to shareholders with 5% or more voting shares.
- Breakdown of advances to suppliers with large amount is as follows:

Name of Suppliers	Closing Balance
Tianjin Tasly Medicine Distribution Group Co., Ltd.	37,151,520.00
Guangdong Dongguan Guoyao Co., Ltd.	24,115,482.54
Shenzhen Sanjiu Pharmaceuticals Trading Co., Ltd.	18,737,663.89
Po Lian Development Co., Ltd.	9,368,995.16
Guangzhou Baiyunshan Guanghua Pharmaceutical Co., Ltd.	8,748,000.00
Guangzhou Baiyunshan Mingxing Pharmaceutical Co., Ltd.	8,375,734.20
Hongkong Fortune Pharmacal Co., Ltd.	7,447,142.34
Prepaid advertisement expenses for the first quarter of 2007	7,211,163.99

### 8. Subsidies receivable

	Closing Balance	Beginning Balance
Export tax refundable	<u>4,611,755.34</u>	<u>3,361,927.18</u>

The closing balance of subsidies receivable increases by 1,250 thousand, representing 37.18% as compared with the beginning balance for the reason that the refund of export tax is comparatively slow, as a result, part of the export tax refundable has not been received by Guangzhou Pharmaceutical Import & Export Corporation, a subsidiary company of the Group.

### 9. Inventories

	Closing Balance		Beginning Balance	
	Provision for Inventory Amount	Write-down	Provision for Inventory Amount	Write-down
Materials in transit	13,608,681.01	—	4,290,795.98	—
Raw materials	103,651,970.24	380,461.88	82,530,152.44	43,562.63
Packaging materials	36,322,516.02	—	28,677,577.80	—
Low-value consumables	1,693,947.30	—	1,482,414.28	—
Goods in stock	941,362,663.45	3,312,178.67	830,892,420.41	1,910,664.20
Finished goods	134,026,271.15	—	91,549,539.57	—
Work-in-process	91,849,534.17	830,677.78	110,259,697.64	—
Materials on consignment for further processing	—	—	402,807.58	—
Consigned goods for sale	33,881.56	—	63,264.17	—
Goods on installment sale	26,082.72	—	—	—
Others	2,594,247.98	—	374,479.02	—
Semi-finished goods	5,796,713.14	—	—	—
	<u>1,330,966,508.74</u>	<u>4,523,318.33</u>	<u>1,150,523,148.89</u>	<u>1,954,226.83</u>

The closing balance of the provision for inventory write-down increases by 2,569 thousand, representing 131.46% as compared with the beginning balance, mainly because the net realizable value of some inventories of the subsidiary companies (Guangzhou Hanfang Modern Chinese Patent Medicine Research & Development Co., Ltd and Guangzhou Baidi Biotechnology Co., Ltd.) is lower than the cost and provision for inventory write-down is accrued accordingly.



# NOTES TO THE FINANCIAL STATEMENTS

## VI. NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (ALL AMOUNTS ARE STATED IN RMB YUAN UNLESS OTHERWISE STATED) (Continued)

### 10. Prepaid expenses

	Beginning Balance	Current Increase	Current Amortization	Closing Balance
Prepayments of insurance premium	741,785.21	949,888.93	1,060,972.12	630,702.02
Road toll	70,250.00	84,413.72	85,250.00	69,413.72
Advertisement expenses	13,502,207.05	16,301,677.46	29,803,884.51	—
Deductible input VAT	105,908,419.91	436,311,383.42	542,125,526.35	94,276.98
Others	442,597.31	2,143,014.36	2,189,752.04	395,859.63
	<u>120,665,259.48</u>	<u>455,790,377.89</u>	<u>575,265,385.02</u>	<u>1,190,252.35</u>

The closing balance of prepaid expenses decreases by 119,475 thousand, representing 99.01% as compared with the beginning balance, mainly because the deductible input VAT is not accrued for the estimated purchase payables; moreover, the prepaid advertisement expenses decrease sharply at the end of year.

### 11. Long-term investment

	Closing Balance		Beginning Balance	
	Amount	Provision for Impairment	Amount	Provision for Impairment
Long-term equity investment	76,967,367.96	1,078,551.23	71,274,292.40	1,078,551.23

#### (1). Long-term equity investment

##### A. Stock investment

Name of the Investee	Type of Stock	Initial Investment Cost	Closing Balance	Provision for Impairment	Beginning Balance
Bank of Communications	share of legal person	393,841.40	393,841.40	—	393,841.40



# NOTES TO THE FINANCIAL STATEMENTS

## VI. NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (ALL AMOUNTS ARE STATED IN RMB YUAN UNLESS OTHERWISE STATED) (Continued)

### 11. Long-term investment (continued)

(1). Long-term equity investment (continued)

B. Other equity investment

a. Equity investment under cost method

Name of the Investee	Term	% of Paid — in Capital of the Investee	Beginning Balance	Movement in the Current Year	Closing Balance
Indonesia Sanyou Industrial Co., Ltd.	2014	50.00%	1,078,551.23	—	1,078,551.23
Shanghai Jiuhe Tang Chinese Medicine Co., Ltd.	2007	29.72%	563,046.60	—	563,046.60
China Everbright Bank	Unlimited	—	10,725,000.00	—	10,725,000.00
Guoyao Group Industrial Co., Ltd.	Unlimited	10.00%	8,000,000.00	—	8,000,000.00
Beijing Imperial Court Cultural Development Co., Ltd.	Unlimited	10.00%	200,000.00	—	200,000.00
Qixing Mazhong Pharmaceutical Co., Ltd.	—	40.00%	362,826.38	—	362,826.38
Guangzhou Chinese Medicine Corporation, Beijing Road Chinese Medicine Bazaar	Unlimited	20.00%	218,399.05	—	218,399.05
East China Pharmaceutical Co., Ltd.	Unlimited	0.016%	126,843.02	—	126,843.02
Nanhai Nanfang Packaging Co., Ltd.	—	21.42%	30,000,000.00	(30,000,000.00)	—
			<u>51,274,666.28</u>	<u>(30,000,000.00)</u>	<u>21,274,666.28</u>

b. Equity investment to subsidiaries under equity method

Name of the Investee	Term	% of Paid-in Capital of the Investee	Movement of Equity interest in the Current Year Including							Closing Balance		Total
			Beginning Balance	Total of the Current Year	Investment	Cost	Amortization Proceeds Recognized	of Differences	Profit Distribution	Initial Cost	Accumulated Movement	
Guangzhou Jing Xiu Tang 1790 Trading Co., Ltd.	Unlimited	51.00%	221,889.71	(183,047.29)	—	(183,047.29)	—	—	—	255,000.00	(216,157.58)	38,842.42



# NOTES TO THE FINANCIAL STATEMENTS

## VI. NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (ALL AMOUNTS ARE STATED IN RMB YUAN UNLESS OTHERWISE STATED) (Continued)

### 11. Long-term investment (continued)

#### (1). Long-term equity investment (continued)

##### c. Equity investment to joint ventures under equity method

Name of the Investee	Term	% of Paid-in Capital of the Investee	Movement of Equity interest in the Current Year						Closing Balance		Total
			Beginning Balance	Including			Amortization of Profit Distribution	Initial Cost	Accumulated Movement		
				Total of the Current Year	Investment Cost	Proceeds Recognized					
Guangzhou Lianjie Computer Technology Co., Ltd.	Unlimited	50.00%	120,576.45	60,765.32	—	60,765.32	—	—	250,000.00	(68,658.23)	181,341.77
Hangzhou Zheda Hanfang Chinese Traditional Medicine Information Engineering Co., Ltd.	Unlimited	44.00%	174,407.66	(69,861.52)	—	(69,861.52)	—	—	440,000.00	(335,453.86)	104,546.14
Golden Eagle Asset Management Co., Ltd.	Unlimited	20.00%	9,757,693.31	(1,394,106.54)	—	(1,394,106.54)	—	—	20,000,000.00	(11,636,413.23)	8,363,586.77
Guangzhou Jihua Health Medical Equipment Co., Ltd.	Unlimited	24.00%	2,094,885.57	(29,104.90)	—	(29,104.90)	—	—	4,200,000.00	(2,134,219.33)	2,065,780.67
Guangzhou Jinshen Pharmaceutical Technology Co., Ltd.	Unlimited	38.25%	82,521.47	(28,518.31)	—	(28,518.31)	—	—	765,000.00	(710,996.84)	54,003.16
Guangzhou Pharmaceutical Football Club Co., Ltd.	Unlimited	46.10%	—	9,181,934.91	9,220,697.50	(38,762.59)	—	—	9,220,697.50	(38,762.59)	9,181,934.91
Guangzhou Nuocheng Bio-product Co., Ltd.	Unlimited	50.00%	—	—	32,000,000.00	—	—	—	32,000,000.00	—	32,000,000.00
Total			12,230,084.46	7,721,108.96	41,220,697.50	(1,499,588.54)	—	—	66,875,697.50	(14,924,504.08)	51,951,193.42

#### (2). Provision for impairment on long-term equity investment

Name of the Investee	Beginning Balance	Current Increase	Current Decrease	Closing Balance
Indonesia Sanyou Industrial Co., Ltd.	1,078,551.23	—	—	1,078,551.23

Beginning from 1997, the Group could not obtain financial information from Indonesia Sanyou Industrial Company Limited and the current situation of the investment is uncontrollable. Based on the principle of prudence, the Group makes provision for impairment at full amount.



# NOTES TO THE FINANCIAL STATEMENTS

## VI. NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (ALL AMOUNTS ARE STATED IN RMB YUAN UNLESS OTHERWISE STATED) (Continued)

### 11. Long-term investment (continued)

(3). Equity investment differences in consolidation variance

Name of the Investee	Initial Amount	Reason	Amortization Term	Current Amortization	Closing Balance
Guangzhou Pangaoshou Natural Health Product Co., Ltd.	1,990,885.94	Difference between purchase payment of equity interest and attributable shareholders' equity	9-13 years	161,853.68	809,267.90
Fujian Guangyao Jieda Co., Ltd.	586,110.87	Difference between purchase payment of equity interest and attributable shareholders' equity	10 years	56,168.96	449,351.66
Guangzhou Baidi Biotechnology Co., Ltd.	454,187.62	Difference between payment for capital increment and attributable shareholders' equity	10 years	45,418.76	325,640.84
Guangzhou Huanye Pharmaceutical Co., Ltd.	992,341.19	Difference between payments for purchase of equity interest & capital increment and attributable shareholders' equity	10 years	99,234.12	595,404.71
Guangxi Ying Kang Pharmaceutical Co., Ltd.	656,216.43	Difference between purchase payment of equity interest and attributable shareholders' equity	10 years	65,621.64	475,756.92
Guangzhou Pharmaceutical Ying Bang Trading Co., Ltd.	911,724.29	Difference between purchase payment of equity interest and attributable shareholders' equity	10 years	91,172.43	653,402.41
Total	5,591,466.34			<u>519,469.59</u>	<u>3,308,824.44</u>



# NOTES TO THE FINANCIAL STATEMENTS

## VI. NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (ALL AMOUNTS ARE STATED IN RMB YUAN UNLESS OTHERWISE STATED) (Continued)

### 12. Fixed assets and accumulated depreciation

(1). Cost and accumulate depreciation of fixed assets

Cost	Beginning Balance	Current Increase	Current Decrease	Closing Balance
Houses & buildings	1,041,727,627.32	67,025,169.25	16,740,714.72	1,092,012,081.85
Machinery equipment	713,407,060.54	32,316,085.16	30,835,346.44	714,887,799.26
Vehicles	90,912,757.67	4,806,753.16	4,780,494.57	90,939,016.26
Electric equipment	31,421,082.26	5,042,763.39	4,850,500.85	31,613,344.80
Office equipment	75,650,516.80	8,938,545.79	4,562,739.71	80,026,322.88
Renovation of fixed assets	21,286,737.11	3,392,151.85	179,000.00	24,499,888.96
	<u>1,974,405,781.70</u>	<u>121,521,468.60</u>	<u>61,948,796.29</u>	<u>2,033,978,454.01</u>
Accumulated depreciation	Beginning Balance	Current Increase	Current Decrease	Closing Balance
Houses & buildings	231,880,104.98	36,535,197.67	770,957.38	267,644,345.27
Machinery equipment	298,675,095.18	58,374,604.87	24,928,595.75	332,121,104.30
Vehicles	60,475,928.48	2,946,664.81	4,242,526.62	59,180,066.67
Electric equipment	17,655,014.01	2,635,136.97	2,281,276.99	18,008,873.99
Office equipment	41,839,104.33	11,397,599.22	4,189,533.45	49,047,170.10
Renovation of fixed assets	8,402,087.15	8,054,480.48	40,850.00	16,415,717.63
	<u>658,927,334.13</u>	<u>119,943,684.02</u>	<u>36,453,740.19</u>	<u>742,417,277.96</u>

(2). Provision for impairment

Provision for Impairment	Beginning Balance	Current Increase	Current Decrease	Closing Balance
Houses & buildings	11,643,357.48	—	730,258.45	10,913,099.03
Machinery equipment	5,581,718.63	136,990.88	—	5,718,709.51
Vehicles	404,199.51	71,600.07	116,230.29	359,569.29
Electric equipment	264,526.78	—	264,526.78	—
Office equipment	8,512.15	—	8,512.15	—
	<u>17,902,314.55</u>	<u>208,590.95</u>	<u>1,119,527.67</u>	<u>16,991,377.83</u>

In the current year, RMB 89,106 thousand of construction work in progress has been transferred into fixed assets.

At the end of the year, fixed assets with costs of 74,706 thousand have been pledged for bank loans.



# NOTES TO THE FINANCIAL STATEMENTS

## VI. NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (ALL AMOUNTS ARE STATED IN RMB YUAN UNLESS OTHERWISE STATED) *(Continued)*

### 13. Construction work in progress

1) Breakdown of construction work in progress is as follows:

Project	Budget	Financing Source	% of Fund Used to Budget
Equipment purchased by Guangzhou Xingqun Pharmaceutical Co., Ltd.	2,594,919.61	Working capital	89
The 3rd phase of preparation workshop project of Guangzhou Xingqun Pharmaceutical Co., Ltd.	6,207,173.98	Working capital	100
Production expansion project for oral liquid of Guangzhou Xingqun Pharmaceutical Co., Ltd.	5,925,715.06	Working capital	112
GMP improvement project on expansion project of grain of Guangzhou Xingqun Pharmaceutical Co., Ltd.	4,388,115.99	Working capital	100
Relocation of Yunpu workshop of Guangzhou Zhongyi Pharmaceutical Co., Ltd.	197,030,000.00	Working capital, loan from financial institute and government appropriation	100
Product technical alteration of Guangzhou Chenliji Pharmaceutical Factory	29,100,000.00	Working capital and stock capital	94
Product show room of Guangzhou Chenliji Pharmaceutical Factory	4,000,000.00	Working capital	107
Conghua base 107construction of 107Guangzhou Hanfang Modern Chinese Patent Medicine Research & Development Co., Ltd.	118,840,000.00	Stock capital and government appropriation	104



# NOTES TO THE FINANCIAL STATEMENTS

## VI. NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (ALL AMOUNTS ARE STATED IN RMB YUAN UNLESS OTHERWISE STATED) (Continued)

### 13. Construction work in progress (continued)

1) Breakdown of construction work in progress is as follows: (continued)

Project	Budget	Financing Source	% of Fund Used to Budget
Equipment installation of Guangzhou Hanfang Modern Chinese Patent Medicine Research & Development Co., Ltd	37,434,000.00	Stock capital and government appropriation	100
Advances for machinery equipment of Guangzhou Jing Xiu Tang Pharmaceutical Co., Ltd.	2,343,821.21	Working capital and loan from financial institute	71
GMP improvement project of Guangzhou Pangaoshou Pharmaceutical Co., Ltd.	109,263,029.14	Loan from financial institute and special fund from treasury bond	102
Payment for 29th F and parking space of Wuyang xincheng Plaza by Guangzhou of Wanglaoji Pharmaceutical Co., Ltd.	10,120,517.19	Working capital	99
ERP upgrade project of Guangzhou Wanglaoji Pharmaceutical Co., Ltd.	2,590,071.50	Working capital	100
GMP preparation workshop project of Guangzhou Wanglaoji Pharmaceutical Co., Ltd.	12,558,146.87	Working capital	100
Organization expenses of Tangangcun project of Guangzhou Pharmaceuticals Corporation	7,230,000.00	Working capital	1





# NOTES TO THE FINANCIAL STATEMENTS

## VI. NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (ALL AMOUNTS ARE STATED IN RMB YUAN UNLESS OTHERWISE STATED) (Continued)

### 13. Construction work in progress (continued)

1) Breakdown of construction work in progress is as follows: (continued)

Project	Budget	Financing Source	% of Fund Used to Budget
GMP Project of Guangzhou Chinese Medicine Corporation, Chinese Medicine Factory	5,400,000.00	Working capital	87
Equipment installation B of Guangzhou Baidi Biotechnology Co., Ltd.	8,000,000.00	Working capital	117
Hydrophobia bacterin construction project of Guangzhou Baidi Biotechnology Co., Ltd.	20,070,000.00	Working capital	98
GMP reconstruction project of Guangxi Ying Kang Pharmaceutical Co., Ltd.	23,000,000.00	Working capital	96
Warehouse project of Guangzhou Qixing Pharmaceutical Co., Ltd.	7,608,128.76	Working capital	100
Others	32,750,920.44	Working capital	—
	<u>646,254,559.75</u>		



# NOTES TO THE FINANCIAL STATEMENTS

## VI. NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (ALL AMOUNTS ARE STATED IN RMB YUAN UNLESS OTHERWISE STATED) (Continued)

### 13. Construction work in progress (continued)

2) The movements of construction work in progress in the current year are as follows:

Project	Beginning Balance	Current Addition	Transferred into Fixed Asset	Other Reduction	Closing Balance
Equipment purchased by Guangzhou Xingqun Pharmaceutical Co., Ltd.	928,445.80	1,383,210.19	1,492,476.78	—	819,179.21
The 3rd phase of preparation workshop project of Guangzhou Xingqun Pharmaceutical Co., Ltd.	325,190.30	178,872.45	504,062.75	—	—
Production expansion project for oral liquid of Guangzhou Xingqun Pharmaceutical Co., Ltd.	5,688,084.20	954,120.52	6,642,204.72	—	—
GMP improvement project on expansion project of grain of Guangzhou Xingqun Pharmaceutical Co., Ltd.	4,188,115.99	213,000.94	—	—	4,401,116.93
Relocation of Yunpu workshop of Guangzhou Zhongyi Pharmaceutical Co., Ltd.	4,833,690.67	2,426,965.43	1,214,715.00	906,560.00	5,139,381.10
Product technical alteration of Guangzhou Chenliji Pharmaceutical Factory	1,135,578.57	4,045,691.91	1,635,557.31	—	3,545,713.17
Product show room of Guangzhou Chenliji Pharmaceutical Factory	—	280,960.07	—	79,960.07	201,000.00



# NOTES TO THE FINANCIAL STATEMENTS

## VI. NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (ALL AMOUNTS ARE STATED IN RMB YUAN UNLESS OTHERWISE STATED) (Continued)

### 13. Construction work in progress (continued)

- 2) The movements of construction work in progress in the current year are as follows:(continued)

Project	Beginning Balance	Current Addition	Transferred into Fixed Asset	Other Reduction	Closing Balance
Conghua base construction of Guangzhou Hanfang Modern Chinese Patent Medicine Research & Development Co., Ltd.	80,764,685.69	12,679,879.43	15,364,004.43	11,126,000.00	66,954,560.69
Equipment installation of Guangzhou Hanfang Modern Chinese Patent Medicine Research & Development Co., Ltd.	30,147,522.55	5,242,850.58	9,782,580.06	—	25,607,793.07
Advances for machinery equipment of Guangzhou Jing Xiu Tang Pharmaceutical Co., Ltd.	522,887.22	1,138,417.58	1,647,804.80	—	13,500.00
GMP improvement project of Guangzhou Pangaoshou Pharmaceutical Co., Ltd.	2,803,288.00	4,353,029.14	5,821,323.54	—	1,334,993.60
Payment for 29th F and parking space of Wuyang xincheng Plaza by Guangzhou Wanglaoji Pharmaceutical Co., Ltd.	4,202,354.79	5,803,890.73	10,006,245.52	—	—
ERP upgrade project of Guangzhou Wanglaoji Pharmaceutical Co., Ltd.	1,251,104.64	1,338,966.86	—	2,590,071.50	—



# NOTES TO THE FINANCIAL STATEMENTS

## VI. NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (ALL AMOUNTS ARE STATED IN RMB YUAN UNLESS OTHERWISE STATED) (Continued)

### 13. Construction work in progress (continued)

- 2) The movements of construction work in progress in the current year are as follows: (continued)

Project	Beginning Balance	Current Addition	Transferred into Fixed Asset	Other Reduction	Closing Balance
GMP preparation workshop project of Guangzhou Wanglaoji Pharmaceutical Co., Ltd.	—	1,636,574.24	1,079,180.07	557,394.17	—
Organization expenses of Tangangcun project of Guangzhou Pharmaceuticals Corporation	—	63,000.00	—	—	63,000.00
GMP Project of Guangzhou Chinese Medicine Corporation, Chinese Medicine Factory	81,031.70	231,717.00	229,437.00	81,031.70	2,280.00
Equipment installation B of Guangzhou Baidi Biotechnology Co., Ltd.	881,369.60	4,155,971.41	2,099,596.48	3,200.00	2,934,544.53
Hydrophobia bacterin construction project of Guangzhou Baidi Biotechnology Co., Ltd.	8,492,483.99	11,135,491.32	14,672,992.00	2,842,028.22	2,112,955.09
GMP reconstruction project of Guangxi Ying Kang Pharmaceutical Co., Ltd.	370,180.00	177,121.00	547,301.00	—	—
Warehouse project of Guangzhou Qixing Pharmaceutical Co., Ltd.	6,195,707.86	1,412,420.90	7,608,128.76	—	—
Others	7,228,683.95	12,443,261.25	8,758,740.32	512,692.76	10,400,512.12
	<u>160,040,405.52</u>	<u>71,295,412.95</u>	<u>89,106,350.54</u>	<u>18,698,938.42</u>	<u>123,530,529.51</u>



# NOTES TO THE FINANCIAL STATEMENTS

## VI. NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (ALL AMOUNTS ARE STATED IN RMB YUAN UNLESS OTHERWISE STATED) (Continued)

### 13. Construction work in progress (continued)

3). Provision for Impairment of Construction Work in Progress

Project	Beginning Balance	Current Increase	Current Decrease	Closing Balance	Accrual Reason
Dust removal project of Guangzhou Zhongyi Pharmaceutical Co., Ltd.	80,000.00	—	—	80,000.00	The said projects have been suspended for a long time and may not be resumed in the foreseeable future.
Anbike Equipment of Guangzhou Jing Xiu Tang Pharmaceutical Co., Ltd.	50,000.00	—	—	50,000.00	
	<u>130,000.00</u>	<u>—</u>	<u>—</u>	<u>130,000.00</u>	

### 14. Intangible assets

1) Breakdown of intangible assets is as follows:

Item	Acquisition Way	Cost	Residual Amortization Month
Land use right of new workshop in Nanzhou Road	Purchase	5,207,786.00	468
Land use right of former workshop in Renmin Road	Purchase	2,686,602.00	468
Land use right of No. 32 of Changhua New Street, Duobao Road and No. 3 of Shiguili, Zhongshanba Road	Purchase	1,392,144.00	163
Land use right of No.19-29 of Ningxiheng Street	Purchase	1,600,547.00	438
Land use right of Guangzhou Yunpu Industry District	Purchase	2,255,182.58	547
Land use right of No. 194 of Beijing Road	Purchase	2,362,581.08	497
Land use right of No. 1688 of Guangzhou Avenue South	Purchase	27,006,173.92	488
Land use right of Conghua Base	Purchase	11,126,000.00	444
Land use right of Songgang Factory	Purchase	3,861,957.56	444
Land use right of Huangqi, Nanhai	Purchase	4,090,000.00	433
Land use right of No. 5 of Panyu Dongsheng Industry District	Purchase	15,947,019.00	468
Land use right of Jiangcun workshop in Guangzhou Baiyun District	Purchase	1,916,553.13	486



# NOTES TO THE FINANCIAL STATEMENTS

## VI. NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (ALL AMOUNTS ARE STATED IN RMB YUAN UNLESS OTHERWISE STATED) (Continued)

### 14. Intangible assets (continued)

1) Breakdown of intangible assets is as follows: (continued)

Item	Acquisition Way	Cost	Residual Amortization Month
Land use right of #4-6 and #10-1 of Shi Er Pu New Street	Purchase	3,509,041.00	367
Land use right of No. 136-138 of He Ping West Road	Purchase	1,535,744.00	367
Land use right of No.103 of Datong Road	Land appraisal appreciation	17,928,863.00	367
Land transfer fee of No.103 of Datong Road	Purchase	1,354,320.00	471
Land transfer fee of No.8 (101,102,201-203,205,305) of Shi Er Pu New Street, Datong Road	Purchase	526,877.00	480
Land transfer fee of No.328 of Beijing Road	Purchase	1,306,988.00	66
Land use right of B area of Xin Zhou Warehouse	Purchase	2,676,141.00	467
Land use right of No.85 of Shangju Road	Purchase	2,973,460.00	396
Land use right of No.12 of Sai Ba Road, Fangcun	Purchase	1,764,522.90	485
Land use right of No.33 of Chi Gang North Street, Xin Gang Central Road	Investment	3,315,488.00	504
Land use right of No. 5-7 of Panyu Dongsheng Industry District	Purchase	2,896,279.62	444
Malotilate emulsion technology	Purchase	1,500,000.00	81
Logistics project software of Huangjinwei warehouse of Guangzhou Pharmaceuticals Corporation	Self-developed	5,491,734.55	29
Trademark of GPC	Investment	3,807,722.31	91
Marketing network and use right of trademark of Hubei Ankang Co., Ltd.	Investment	1,200,000.00	87
ERP Software	Purchase	2,590,071.50	56
Others		11,311,337.62	15~624
		<u>145,141,136.77</u>	



# NOTES TO THE FINANCIAL STATEMENTS

## VI. NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (ALL AMOUNTS ARE STATED IN RMB YUAN UNLESS OTHERWISE STATED) (Continued)

### 14. Intangible assets (continued)

(2). The movements of intangible assets in the current year are as below:

Item	Beginning Balance	Current Increase	Current Amortization	Accumulated Amortization	Closing Balance
Land use right of new workshop in Nanzhou Road	3,610,122.97	906,740.00	92,155.74	783,078.77	4,424,707.23
Land use right of former workshop in Renmin Road	2,201,098.97	—	54,828.61	540,331.64	2,146,270.36
Land use right of No. 32 of Changhua New Street, Duobao Road and No. 3 of Shiguili, Zhongshanba Road	1,064,468.00	—	68,664.00	396,340.00	995,804.00
Land use right of No.19-29 of Ningxiheng Street	1,305,233.99	—	34,420.36	329,733.37	1,270,813.63
Land use right of Guangzhou Yunpu Industry District	2,162,344.86	—	46,418.88	139,256.60	2,115,925.98
Land use right of No. 194 of Beijing Road	2,009,393.91	—	47,251.62	400,438.79	1,962,142.29
Land use right of No. 1688 of Guangzhou Avenue South	22,505,144.92	—	540,123.48	5,041,152.48	21,965,021.44
Land use right of Conghua Base	—	11,126,000.00	292,789.47	292,789.47	10,833,210.53
Land use right of Songgang Factory	1,686,622.21	—	44,384.76	2,219,720.11	1,642,237.45
Land use right of Huangqi, Nanhai	3,064,361.90	—	82,634.52	1,108,272.62	2,981,727.38
Land use right of No. 5 of Panyu Dongsheng Industry District	13,095,047.24	—	318,940.38	3,170,912.14	12,776,106.86
Land use right of Jiangcun workshop in Guangzhou Baiyun District	1,413,215.31	—	34,056.24	537,394.06	1,379,159.07



# NOTES TO THE FINANCIAL STATEMENTS

## VI. NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (ALL AMOUNTS ARE STATED IN RMB YUAN UNLESS OTHERWISE STATED) (Continued)

### 14. Intangible assets (continued)

(2). The movements of intangible assets in the current year are as below: (continued)

Item	Beginning Balance	Current Increase	Current Amortization	Accumulated Amortization	Closing Balance
Land use right of #4-6 and #10-1 of Shi Er Pu New Street	2,995,329.75	—	94,839.00	608,550.25	2,900,490.75
Land use right of No. 136-138 of He Ping West Road	1,310,916.80	—	41,506.56	266,333.76	1,269,410.24
Land use right of No.103 of Datong Road	13,801,592.96	—	495,272.40	4,622,542.44	13,306,320.56
Land transfer fee of No.103 of Datong Road	—	1,354,320.00	25,393.50	25,393.50	1,328,926.50
Land transfer fee of No.8 (101,102,201-203,205,305) of Shi Er Pu New Street, Datong Road	—	526,877.00	1,097.67	1,097.67	525,779.33
Land transfer fee of No.328 of Beijing Road	1,034,699.00	—	32,674.68	304,963.68	1,002,024.32
Land use right of B area of Xin Zhou Warehouse	2,180,043.94	—	42,483.60	538,580.66	2,137,560.34
Land use right of No.85 of Shangjiu Road	2,314,055.82	—	66,076.92	725,481.10	2,247,978.90
Land use right of No.12 of Sai Ba Road, Fangcun	1,462,950.55	—	35,290.44	336,862.79	1,427,660.11
Land use right of No.33 of Chi Gang North Street, Xin Gang Central Road	1,509,547.68	—	35,105.76	1,841,046.08	1,474,441.92
Land use right of No. 5-7 of Panyu Dongsheng Industry District	2,145,856.70	—	60,781.20	811,204.12	2,085,075.50





# NOTES TO THE FINANCIAL STATEMENTS

## VI. NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (ALL AMOUNTS ARE STATED IN RMB YUAN UNLESS OTHERWISE STATED) (Continued)

### 14. Intangible assets (continued)

(2). The movements of intangible assets in the current year are as below: (continued)

Item	Beginning Balance	Current Increase	Current Amortization	Accumulated Amortization	Closing Balance
Malotilate emulsion technology	1,162,500.00	—	150,000.00	487,500.00	1,012,500.00
Logistics project software of Huangjinwei warehouse of Guangzhou Pharmaceuticals Corporation	3,784,073.17	100,000.00	1,087,962.23	2,695,623.61	2,796,110.94
Trademark of GPC	3,268,294.97	—	380,772.24	920,199.58	2,887,522.73
Marketing network and use right of trademark of Hubei Ankang Co., Ltd.	990,000.00	—	120,000.00	330,000.00	870,000.00
ERP Software	—	2,590,071.50	215,839.29	215,839.29	2,374,232.21
Others	7,566,919.64	1,414,465.00	1,241,846.90	3,571,799.88	7,739,537.74
	<u>99,643,835.26</u>	<u>18,018,473.50</u>	<u>5,783,610.45</u>	<u>33,262,438.46</u>	<u>111,878,698.31</u>

(3). Provision for impairment of intangible assets

Project	Closing Balance	Beginning Balance	Reason
Land use right of B area of Xin Zhou -20Warehouse	<b>480,700.24</b>	480,700.24	Accrued for the difference between the lower estimated recoverable amount and the book value
Langcheng financial software	—	485,451.22	The provision for impairment is transferred out upon disposal of Langcheng software of Guangzhou Pharmaceuticals Corporation, the subsidiary of the Group
	<u><b>480,700.24</b></u>	<u>966,151.46</u>	



# NOTES TO THE FINANCIAL STATEMENTS

## VI. NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (ALL AMOUNTS ARE STATED IN RMB YUAN UNLESS OTHERWISE STATED) (Continued)

### 15. Long-term prepayment

- 1) Breakdown of long-term prepayment is as follows:

Item	Estimated Amortization Period	Cost
Renovation expense	5 Years	28,318,276.43
Installation of telephone	5 Years	469,000.00
ERP system	5 Years	6,519,667.86
Computer system	5 Years	1,432,382.47
GMP project improvement	5 Years	893,627.82
Medical fund for retired staff	5 Years	1,864,500.00
Transitional medical fund for retired staff	10 Years	3,269,676.46
CI Design	10 Years	331,000.00
Chinese-medicine protection fee of Weichangning	7 Years	683,679.70
Others	2-5 years	4,545,210.44
		<u>48,327,021.18</u>

- 2) The movements of long-term prepayment during the current year are as below:

Item	Beginning Balance	Current Addition	Current Amortization	Accumulated Amortization	Closing Balance
Renovation	8,374,226.33	1,132,485.30	4,947,171.99	23,758,736.79	4,559,539.64
Installation of telephone	12,159.34	—	12,159.34	469,000.00	—
ERP system	827,499.40	725,480.00	1,434,101.06	6,400,789.52	118,878.34
Computer system	704,243.60	—	344,813.07	1,072,951.94	359,430.53
GMP project improvement	457,507.02	95,800.00	126,909.55	467,230.35	426,397.47
Medical fund for retired staff	112,783.09	—	112,783.09	1,864,500.00	—
Transitional medical fund for retired staff	1,959,417.34	—	349,486.42	1,659,745.54	1,609,930.92
CI Design	264,800.00	—	33,100.00	99,300.00	231,700.00
Chinese-medicine protection fee of Weichangning	553,679.70	130,000.00	65,112.35	65,112.35	618,567.35
Others	1,765,266.87	424,304.34	669,622.94	3,025,262.17	1,519,948.27
	<u>15,031,582.69</u>	<u>2,508,069.64</u>	<u>8,095,259.81</u>	<u>38,882,628.66</u>	<u>9,444,392.52</u>

- 3) The closing balance of long-term prepayment decreases by 5,587 thousand, representing 37.17% as compared with the beginning balance, mainly because there is less addition in the current year than that of last year.



# NOTES TO THE FINANCIAL STATEMENTS

## VI. NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (ALL AMOUNTS ARE STATED IN RMB YUAN UNLESS OTHERWISE STATED) (Continued)

### 16. Short-term borrowings

	Closing Balance	Beginning Balance
Loan by credit	330,586,050.00	45,586,020.00
Loan by mortgage and pledge	169,613,019.88	254,199,348.60
Loan by guaranty	388,000,000.00	568,000,000.00
	<u>888,199,069.88</u>	<u>867,785,368.60</u>

Please refer to point 2 of Note X. Commitments for more details of mortgage and pledge.

### 17. Notes payable

Item	Closing Balance	Beginning Balance
Bank acceptance bill	125,706,757.45	34,728,030.03
Trade acceptance bill	80,993,260.83	51,280,033.35
	<u>206,700,018.28</u>	<u>86,008,063.38</u>

The closing balance of notes payable increases by 120,692 thousand, representing 140.33% as compared with the beginning balance, mainly because Guangzhou Pharmaceuticals Corporation, the subsidiary of the Group, uses more bills for settlement.

### 18. Accounts payable

	Closing Balance	Beginning Balance
Goods payment	<u>861,098,479.40</u>	<u>869,696,059.12</u>

Of the closing balance, no account is due to shareholders with 5% or more voting shares.

### 19. Advances from customers

	Closing Balance	Beginning Balance
Advances from customers	<u>47,942,658.87</u>	<u>31,129,313.34</u>

1). Among the closing balance, no advance is from the shareholders with 5% or more voting shares.

2). The closing balance of advances from customers increases by 16,813 thousand, representing 54.01% as compared with the beginning balance, mainly because that Guangzhou Pharmaceuticals Corporation, the subsidiary of the Group, requires advanced payment before delivery of goods for new customers; furthermore, Guangzhou Wanglaoji Pharmaceutical Co., Ltd. has increased its sales of food which requires advances from customers.



# NOTES TO THE FINANCIAL STATEMENTS

## VI. NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (ALL AMOUNTS ARE STATED IN RMB YUAN UNLESS OTHERWISE STATED) (Continued)

### 20. Other payables

	Closing Balance	Beginning Balance
Security money, deposit and down payment	20,278,536.63	14,442,530.49
Technology development expenses	—	2,348,999.17
Labor union outlay	1,350,875.57	1,739,109.68
Staff educational outlay	11,699,113.64	11,878,877.69
Current accounts with external companies	28,009,967.50	32,182,833.66
Government levies and surcharges	89,045.76	292,400.67
Payables to staff	699,884.65	2,005,242.03
Labor insurance	771,563.17	1,208,250.77
Housing allowance for staff	15,694,146.80	19,276,096.54
Staff bonus and welfare fund	1,181,965.00	2,460,141.54
Payables to Guangzhou Pharmaceutical Holdings Limited	16,993,838.95	25,468,086.39
Payables to Bank of Communications Guangzhou Branch (Collected on behalf)	100,605,883.54	58,923,524.00
Operators' incentive fund	30,811.10	1,672,340.18
Estimated payment for fixed assets	17,546,691.17	6,880,152.57
Postponable taxes payment	8,253,025.94	8,253,025.94
Others	25,533,032.09	2,112,587.69
	<b>248,738,381.51</b>	<b>191,144,199.01</b>

- 1). Among the closing balance, the payable to the shareholders with 5% or more voting shares is that payable to the Holding with the amount of 16,994 thousand.
- 2). The closing balance of other payables increases by 57,594 thousand, being 30.13% as compared with the beginning balance, mainly because that the payable for discounted notes receivable of Guangzhou Pharmaceuticals Corporation increases dramatically, i.e., 41,682 thousand; and the estimated payment for fixed assets increases by 10,667 thousand.

### 21. Dividends payable

	Closing Balance	Beginning Balance
Dividends to minor shareholders	25,871.16	1,753.52
Dividends to overseas public shares	14,618.59	24,739.37
State shares	1,469,754.37	—
	<b>1,510,244.12</b>	<b>26,492.89</b>

The closing balance of dividends payable increases by 1,484 thousand, being 5600.56% as compared with the beginning balance, mainly because dividends to China Great Wall Asset Management Corporation has been accrued but not yet paid.



# NOTES TO THE FINANCIAL STATEMENTS

## VI. NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (ALL AMOUNTS ARE STATED IN RMB YUAN UNLESS OTHERWISE STATED) (Continued)

### 22. Taxes payable

	Closing Balance	Beginning Balance
Value added tax	(11,853,188.28)	(7,110,797.17)
Business tax	551,838.11	537,448.97
Enterprise income tax	43,892,906.38	25,360,418.09
Urban maintenance & construction tax	719,208.21	933,086.59
Property tax	226,876.59	335,299.76
Withholding tax	3,046,580.97	4,111,600.03
Others	219,816.04	210,357.34
	<u>36,804,038.02</u>	<u>24,377,413.61</u>

The closing balance of taxes payable increases by 12,427 thousand, representing 50.98% as compared with the beginning balance, mainly because sales increases in the current year and taxes increases accordingly.

### 23. Other liabilities

Item	Standard of Accrual and Payment	Closing Balance	Beginning Balance
Education surcharge	1)	304,107.76	402,995.72
Flood prevention levy	2)	3,488,658.83	3,175,229.22
Others		13,992.52	50,432.72
		<u>3,806,759.11</u>	<u>3,628,657.66</u>

1) Education surcharge is paid at 3% of the payable amount of VAT, business tax and consumption tax.

2) Flood prevention levy is paid at 0.05% of taxable revenue (on VAT, business tax, consumption tax and resources tax) for commercial enterprises, 0.09% for foreign invested enterprises, and 0.13% for other enterprises.

### 24. Accrued expenses

Item	Closing balance	Beginning balance
Interest on loan	1,832,246.32	1,255,628.75
Rental	1,480,079.48	1,836,899.84
Agency expenses	2,261,000.00	2,430,164.70
Advertising expenses	2,781,602.22	3,835,218.44
Transportation costs	2,334,385.33	673,397.84
Electricity and water costs	806,832.35	759,970.24
Service fee	300,000.00	—
Others	1,597,146.38	3,428,821.77
	<u>13,393,292.08</u>	<u>14,220,101.58</u>



# NOTES TO THE FINANCIAL STATEMENTS

## VI. NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (ALL AMOUNTS ARE STATED IN RMB YUAN UNLESS OTHERWISE STATED) (Continued)

### 25. Long-term liabilities due within one year

Item	Closing balance	Beginning balance
Loan by credit	—	50,000,000.00

### 26. Long-term payables

	Content	Closing Balance	Beginning Balance
Guangzhou Finance Bureau	State dividends	2,149,157.22	2,170,889.31
Finance Department of Guangxi Zhuang Municipality	Payable for transferring equity interest	2,264,426.47	2,264,426.47
Others		281,411.85	281,412.43
		<b>4,694,995.54</b>	<b>4,716,728.21</b>

### 27. Special payables

	Closing Balance	Beginning Balance
Government appropriations as science and technology fund	62,302,433.01	45,758,891.04
Interest subsidies of government	2,563,697.50	3,286,905.00
Special fund for technology export	408,727.20	506,678.78
GMP relocation project-draining project	910,000.00	556,874.56
Sewage treatment project	264,000.00	—
Others	10,000.00	—
	<b>66,458,857.71</b>	<b>50,109,349.38</b>

The closing balance of special payables increases by 16,350 thousand, being 32.63% as compared with the beginning balance, mainly because 13,000 thousand appropriated from government to Guangzhou Hanfang Modern Chinese Patent Medicine Research & Development Co., Ltd., the subsidiary of the Group, was recorded in the "Other Payables the Holding" last year and transferred into this account in the current year.



# NOTES TO THE FINANCIAL STATEMENTS

## VI. NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (ALL AMOUNTS ARE STATED IN RMB YUAN UNLESS OTHERWISE STATED) (Continued)

### 28. Share capital

	Beginning Balance	Proportion %	Current Increase (+), Decrease (-)			Closing Balance	Proportion %
			Share Discretion Reformation	Dividend Shares	Issue of New Shares		
<b>1. Non-circulating shares</b>							
(1) Initiators' shares	513,000,000.00	63.26%	(513,000,000.00)	—	— (513,000,000.00)	—	—
Including:							
Shares held by the State	513,000,000.00	63.26%	(513,000,000.00)	—	— (513,000,000.00)	—	—
Including: State shares	513,000,000.00	63.26%	(513,000,000.00)	—	— (513,000,000.00)	—	—
State-owned legal person shares	—	—	—	—	—	—	—
Shares held by domestic legal persons	—	—	—	—	—	—	—
Shares held by overseas legal persons	—	—	—	—	—	—	—
Shares held by natural persons	—	—	—	—	—	—	—
(2) Collecting legal person shares	—	—	—	—	—	—	—
(3) Employees' shares	—	—	—	—	—	—	—
(4) Preferred shares or others	—	—	—	—	—	—	—
Including: Transfer right share	—	—	—	—	—	—	—
<b>Total of non-circulating shares</b>	<b>513,000,000.00</b>	<b>63.26%</b>	<b>(513,000,000.00)</b>	<b>—</b>	<b>— (513,000,000.00)</b>	<b>—</b>	<b>—</b>
<b>2. Circulating shares with limit on sales</b>							
Shares held by the State	—	—	489,600,000.00	—	— 489,600,000.00	489,600,000.00	60.38%
Shares held by state-owned legal persons	—	—	—	—	—	—	—
Shares held by other domestic legal persons	—	—	—	—	—	—	—
Shares held by domestic natural persons	—	—	—	—	—	—	—
Shares held by overseas legal person and overseas natural persons	—	—	—	—	—	—	—
<b>Total of circulating shares with limit on sales</b>	<b>—</b>	<b>—</b>	<b>489,600,000.00</b>	<b>—</b>	<b>— 489,600,000.00</b>	<b>489,600,000.00</b>	<b>60.38%</b>
<b>3. Circulating shares without limit on sales</b>							
A shares	78,000,000.00	9.62%	23,400,000.00	—	— 23,400,000.00	101,400,000.00	12.50%
Foreign investment shares going public overseas	219,900,000.00	27.12%	—	—	—	219,900,000.00	27.12%
<b>Total of circulating shares without limit on sales</b>	<b>297,900,000.00</b>	<b>36.74%</b>	<b>23,400,000.00</b>	<b>—</b>	<b>— 23,400,000.00</b>	<b>321,300,000.00</b>	<b>39.62%</b>
<b>4. Total of shares</b>	<b>810,900,000.00</b>	<b>100.00%</b>				<b>810,900,000.00</b>	<b>100.00%</b>

In April 2006, the Company implemented the share discretion reformation. The non-circulating shareholders agreed to pay the considerations to the circulating ones so that all their holding non-circulating shares could be circulated in the A share market. The detailed plan is as follows: the holders of the circulating A shares were paid 3 shares for every 10 shares. Therefore, 23,400,000 state shares were paid to the A shareholders in the reporting period.



# NOTES TO THE FINANCIAL STATEMENTS

## VI. NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (ALL AMOUNTS ARE STATED IN RMB YUAN UNLESS OTHERWISE STATED) (Continued)

### 29. Capital surplus

	Beginning Balance	Current Increase	Current Decrease	Closing Balance
Share premium	914,006,770.47	—	—	914,006,770.47
Reserve of donated non-cash assets	2,605,049.96	97,479.07	—	2,702,529.03
Receipt of cash donation	219,652.84	—	—	219,652.84
Equity investment reserve	19,115,775.92	16,688.40	—	19,132,464.32
Transfer-in from government appropriations	19,203,964.37	2,455,797.33	—	21,659,761.70
Exchange difference on foreign currency capital	373,893.09	—	—	373,893.09
Other capital surplus	193,928,649.01	1,196,749.50	—	195,125,398.51
	<u>1,149,453,755.66</u>	<u>3,766,714.30</u>	<u>—</u>	<u>1,153,220,469.96</u>

The current increase of capital surplus amounts to 3,767 thousand, mainly resulting from:

- 1). Upon the completion of research and development projects, the governmental appropriation of 2,456 thousand is transferred from special payables to capital surplus.
- 2). 251 thousand of payables that do not need to repay is recorded as other capital surplus.
- 3). The surplus between the fixed assets transferred out and the equity interest obtained, i.e., 238 thousand, is recorded as other capital surplus.
- 4). Upon disposal of fixed assets that were previously appraised to be depreciated, the devalue amount of 708 thousand is transferred into "Other Capital Surplus".

### 30. Surplus reserve

	Beginning Balance	Current Increase	Current Decrease	Closing Balance
Statutory surplus reserve	253,770,252.85	229,257,111.49	859,831.47	482,167,532.87
Statutory public welfare fund	179,461,575.56	—	179,461,575.56	—
Discretionary surplus reserve	129,038,018.69	32,497,879.87	614,070.80	160,921,827.76
Transfer-in from tax exemption and reduction	4,973,493.07	—	—	4,973,493.07
	<u>567,243,340.17</u>	<u>261,754,991.36</u>	<u>180,935,477.83</u>	<u>648,062,853.70</u>

- 1). Pursuant to the new Corporation Law and the document with reference CQ[2006]No.67, companies should manage and use the balance of statutory public welfare fund as at December 31, 2005 as surplus reserve. The Group has transferred the statutory public welfare fund with an amount of 179,049 thousand into statutory surplus reserve.
- 2). The wholesale department of Medicine Powder and Chinese Medicine of Guangzhou Chinese Medicine Corporation, which is a subsidiary of the Group, has finished its liquidation and thus transferred the balance of statutory surplus reserve of 860 thousand, statutory public welfare fund of 413 thousand and discretionary surplus reserve of 614 thousand, totally amounting to 1,887 thousand, into the retained earnings.





# NOTES TO THE FINANCIAL STATEMENTS

## VI. NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (ALL AMOUNTS ARE STATED IN RMB YUAN UNLESS OTHERWISE STATED) (Continued)

### 31. Retained earnings

- 1) Please refer to Statement 3 for the details of retained earnings.
- 2) The profit distribution policy of the Group is stated in Note V.
- 3) Transfer from others: please refer to point 2) of Note VI. 30 for more details.

### 32. Revenue from and cost of main operations

#### Business Segment

Item	Revenue from Main Operations		Cost of Main Operations	
	2006	2005	2006	2005
(1) Manufacture and sales	<b>2,412,183,229.62</b>	2,141,675,546.01	<b>1,153,545,810.65</b>	1,025,242,616.80
(2) Trade	<b>7,828,820,275.59</b>	6,884,664,887.49	<b>7,318,682,153.73</b>	6,447,731,715.37
Including:				
Wholesale	<b>7,267,373,285.53</b>	6,345,287,623.97	<b>6,845,735,018.70</b>	5,987,651,996.27
Retail	<b>335,871,687.23</b>	318,669,363.09	<b>263,182,691.36</b>	254,472,428.57
Import & Export	<b>225,575,302.83</b>	220,707,900.43	<b>209,764,443.67</b>	205,607,290.53
Total	<b>10,241,003,505.21</b>	9,026,340,433.50	<b>8,472,227,964.38</b>	7,472,974,332.17

In the current year, revenue from sales to the top five customers totals up to 798,426 thousand, representing 7.80 of the Group's total revenue from main operations.

### 33. Sales tax and levies

	2006	2005
Business tax	<b>443,108.60</b>	330,591.43
Urban maintenance & construction tax	<b>17,537,753.08</b>	17,011,021.98
Education surcharge	<b>6,615,421.08</b>	7,234,655.10
Land appreciation tax	<b>916,731.95</b>	—
Others	<b>77,967.39</b>	37,642.30
	<b>25,590,982.10</b>	24,613,910.81

### 34. Profit from other operations

	2006	2005
1) Revenue from other operations		
Lease of assets	<b>34,863,027.80</b>	38,439,132.25
Sales of materials	<b>4,550,290.85</b>	1,179,133.28
Agency charges	<b>140,965.74</b>	370,322.72
Income of member stores	<b>640,286.19</b>	358,055.79
Product promotion fees	<b>5,172,221.51</b>	1,801,944.10
Income from trademark	<b>2,192,016.22</b>	898,860.94
Consultancy income	<b>1,355,109.43</b>	3,289,521.74
Others	<b>5,236,536.11</b>	4,793,912.00
Subtotal	<b>54,150,453.85</b>	51,130,882.82



# NOTES TO THE FINANCIAL STATEMENTS

## VI. NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (ALL AMOUNTS ARE STATED IN RMB YUAN UNLESS OTHERWISE STATED) (Continued)

### 34. Profit from other operations (continued)

2) Cost of other operations		
Lease of assets	427,808.68	333,802.26
Sales of materials	3,702,886.08	857,670.11
Taxes and levies	6,137,902.00	5,580,864.82
Others	2,373,865.88	1,057,014.22
	<u>12,642,462.64</u>	<u>7,829,351.41</u>
Subtotal	12,642,462.64	7,829,351.41
Profit from other operations	<u>41,507,991.21</u>	<u>43,301,531.41</u>

### 35. Financial expenses

Item	2006	2005
Interest expenses	46,851,236.96	45,066,718.52
Less: Interest income	9,067,614.54	9,329,134.72
Exchange loss or gain	82,118.30	(304,387.58)
Financial institution charges	7,470,051.82	7,665,275.35
Others	23,807.10	—
	<u>45,359,599.64</u>	<u>43,098,471.57</u>

### 36. Investment income

#### 1). Current Year:

Category	Proceeds on Fund Investment	Proceeds on Debenture Investment	Equity Investment Income Recognized under Cost Method	Equity Investment Income Recognized under Equity Method	Proceeds on Transfer of Equity Interest	Provision for Impairment	Total
Short-term investment	4,976,837.00	(1,136,147.06)	—	—	—	1,048,000.00	4,888,689.94
Long-term equity investment	—	—	4,553,865.17	(2,218,793.84)	(118,223.76)	—	2,216,847.57
	<u>4,976,837.00</u>	<u>(1,136,147.06)</u>	<u>4,553,865.17</u>	<u>(2,218,793.84)</u>	<u>(118,223.76)</u>	<u>1,048,000.00</u>	<u>7,105,537.51</u>

#### 2). Last Year:

Category	Proceeds on Debenture Investment	Equity Investment Income Recognized under Cost Method	Equity Investment Income Recognized under Equity Method	Proceeds on Transfer of Equity Interest	Provision for Impairment	Total
Short-term investment	(517,355.66)	—	—	—	(7,659,480.00)	(8,176,835.66)
Long-term equity investment	—	3,705,374.86	(3,596,294.73)	4,674.88	—	113,755.01
	<u>(517,355.66)</u>	<u>3,705,374.86</u>	<u>(3,596,294.73)</u>	<u>4,674.88</u>	<u>(7,659,480.00)</u>	<u>(8,063,080.65)</u>

The current investment income is up by 15,169 thousand than that of last year, mainly because the provision for impairment of the treasury bond, which is under trusteeship to Nanfang Security Co., Ltd., was accrued at 7,659 thousand last year; Moreover, net income from selling the Golden Eagle Fund is 4,977 thousand in the current year.



# NOTES TO THE FINANCIAL STATEMENTS

## VI. NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (ALL AMOUNTS ARE STATED IN RMB YUAN UNLESS OTHERWISE STATED) (Continued)

### 37. Revenue from subsidies

Category	2006	2005
Interest subsidy for export	130,313.00	189,521.00
Governmental subsidies for employing certain staff	503,739.06	—
Government bounty	—	200,000.00
Special fund to encourage science and technology for development of trading	150,000.00	330,935.65
Special fund for export of technology	406,192.15	—
	<u>1,190,244.21</u>	<u>720,456.65</u>

During the current year, the amount of revenue from subsidies increases by 470 thousand, being 65.21% as compared with that of last year, mainly because Guangzhou Pangaoshou Pharmaceutical Co., Ltd., and Guangxi Yingkang Pharmaceutical Co., Ltd., both are the subordinates to the Group, have received 500 thousand for special funds and 500 thousand for governmental subsidies for employing certain staff respectively.

### 38. Non-operating income

Category	2006	2005
Net profit from disposal of fixed assets	314,639.45	744,260.39
Sales of obsolete materials	39,967.11	66,348.00
Fine and overdue payment	134,320.83	114,005.09
Compensation for dismantling	3,815,957.83	490,216.73
Fixed assets surplus	—	3,754,778.00
Others	892,736.11	1,024,904.10
	<u>5,197,621.33</u>	<u>6,194,512.31</u>

### 39. Non-operating expenses

	2006	2005
Net loss on disposal of fixed assets	2,832,472.14	1,554,441.54
Provision for impairment of assets	49,755.09	1,114,672.07
Reversal of provision for impairment of fixed assets	(95,632.63)	(6,642,181.93)
Donation	1,416,338.03	1,460,141.69
Fine and overdue payment	3,959,057.75	1,119,962.03
Family control bonus	506,549.48	595,462.83
Sponsor expenditures	317,962.20	676,228.88
Dimission compensation	11,100.00	336,611.40
Extraordinary losses	296,549.16	—
Others	589,399.88	209,487.63
	<u>9,883,551.10</u>	<u>424,826.14</u>

The current non-operating expenses increase by 9,459 thousand, representing 2,226.49% as compared with those of last year, mainly because the provision for the impairment of fixed assets of 6,642 thousand was reversed last year.



# NOTES TO THE FINANCIAL STATEMENTS

## VI. NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (ALL AMOUNTS ARE STATED IN RMB YUAN UNLESS OTHERWISE STATED) (Continued)

### 40. Other cash received relating to operating activities, amounting to 95,245 thousand

Main Item	Amount RMB'000
Non-operating income	4,883
Revenue from other operations	54,150
Financial special appropriations	11,107
Interest income	9,068

### 41. Other cash paid relating to operating activities, amounting to 819,576 thousand Including:

Main Item	Amount RMB'000
Operating expenses paid in cash	575,110
General & administration expenses paid in cash	227,517
Financial expenses - bank charges	7,470

### 42. Other cash received relating to investing activities, amounting to 6,760 thousand Including:

Main Item	Amount RMB'000
Fugao Pharmaceutical Co., Ltd.	6,395

### 43. Other cash paid relating to investing activities, amounting to 1,342 thousand Including:

Main Item	Amount RMB'000
Taxes arising from interest on entrust loans	1,087

### 44. Other cash received relating to financing activities, amounting to 355,235 thousand

Main Item	Amount RMB'000
Discounted bills	355,234

### 45. Other cash paid relating to financing activities, amounting to 313,553 thousand

Main Item	Amount RMB'000
Discounted bills	313,553



# NOTES TO THE FINANCIAL STATEMENTS

## VII. NOTES TO THE ACCOUNTS OF THE COMPANY (ALL AMOUNTS ARE STATED IN RMB YUAN UNLESS OTHERWISE STATED)

### 1. Accounts Receivable

(1) Aging analysis

Closing balance				
Aging	Amount	% of the Total	Bad Debts Provision	Accrual Provision of Bad Debt Proportion
Within 1 year	26,229,457.78	100%	262,294.58	1%
Beginning Balance				
Aging	Amount	% of the Total	Bad Debts Provision	Accrual Provision of Bad Debt Proportion
Within 1 year	—	—	—	—

Among the aforesaid balance, no account is due from shareholders holding 5% or more voting shares.

- (2) At the end of the year, 8,238 thousand is owed by the top five customers with largest amount, representing 31.40% of the total balance.
- (3) The closing balance of accounts receivable increases by 26,229 thousand, being 100% as compared with the beginning balance, mainly because the Yingbang Branch of the Company that engages in sale of medicine is set up in the current year.

### 2 Other receivables

(1) Aging analysis of other receivable as at December 31, 2006

Closing balance				
Aging	Amount	% of the Total	Bad Debts Provision	Accrual Provision of Bad Debt Proportion
Within 1 year	203,501,300.70	93.52%	679.36	—
2~3 years	42,627.00	0.02%	—	—
3~4 years	13,545,440.56	6.23%	9,752,600.00	72.00%
Over 5 years	502,843.54	0.23%	502,043.54	99.84%
	<u>217,592,211.80</u>	<u>100.00%</u>	<u>10,255,322.90</u>	



# NOTES TO THE FINANCIAL STATEMENTS

## VII. NOTES TO THE ACCOUNTS OF THE COMPANY (ALL AMOUNTS ARE STATED IN RMB YUAN UNLESS OTHERWISE STATED) (Continued)

### 2 Other receivables (Continued)

(1) Aging analysis of other receivables at December 31, 2006 (Continued)

Aging	Beginning Balance			Accrual Provision of Bad Debt Proportion
	Amount	% of the Total	Bad Debts Provision	
Within 1 year	5,777,788.87	3.45%	—	—
1~2 years	5,098,010.89	3.04%	—	—
2~3 years	33,870,656.54	20.23%	—	—
3~4 years	50,644,000.00	30.25%	—	—
4~5 years	21,498,596.76	12.84%	—	—
Over 5 years	50,544,562.54	30.19%	502,043.54	0.99%
	<u>167,433,615.60</u>	100.00%	<u>502,043.54</u>	

(2) The five largest amounts of other receivables add up to 182,435 thousand, accounting for 83.84% of the total.

(3) Among the aforesaid balance, other receivables due from shareholders holding 5% or more voting shares represent that dues from the Holding with an amount of 3,792 thousand.

### 3 Long-term equity investments

Item	Closing Balance		Beginning Balance	
	Amount	Provision for Impairment	Amount	Provision for Impairment
Long-term equity investment	<u>2,132,494,302.74</u>	—	<u>2,025,934,634.58</u>	—

(1) Equity investment under cost method

Name of the Investee	Term	% of Paid-in Capital of the Investee	Beginning Balance	Movement in the Current Year	Closing Balance
China Everbright Bank	Unlimited	—	10,725,000.00	—	10,725,000.00
Guoyao Group Industry Corporation	Unlimited	10.00%	8,000,000.00	—	8,000,000.00
Beijing Imperial Court Cultural Development Co., Ltd	Unlimited	10.00%	200,000.00	—	200,000.00
Nanhai Nanfang Packaging Co., Ltd.	—	21.42%	30,000,000.00	(30,000,000.00)	—
Total			<u>48,925,000.00</u>	<u>(30,000,000.00)</u>	<u>18,925,000.00</u>



# NOTES TO THE FINANCIAL STATEMENTS

## VII. NOTES TO THE ACCOUNTS OF THE COMPANY (ALL AMOUNTS ARE STATED IN RMB YUAN UNLESS OTHERWISE STATED) (Continued)

### 3 Long-term equity investments (Continued)

#### (2) Equity investment to subsidiaries under equity method

Name of the Investee	Term	% of Paid-in Capital of the Investee	Beginning Balance		Movement of Equity Interest in the Current Year				Closing Balance		Total
			Balance	Total of the Current Year	Investment Cost	Including Proceeds Recognized	Amortization of Difference	Profit Distribution	Initial Cost	Accumulated Movement	
Guangzhou Xinggun Pharmaceutical Co., Ltd	Unlimited	88.99%	192,115,850.29	8,522,322.43	—	25,445,601.79	—	(16,923,279.36)	125,322,318.71	75,315,854.01	200,638,172.72
Guangzhou Zhongyi Pharmaceutical Company Limited	Unlimited	100.00%	347,551,118.34	71,710,466.70	36,814,400.00	79,792,887.80	—	(44,896,821.10)	193,023,721.79	226,237,863.25	419,261,585.04
Guangzhou Chenliji Pharmaceutical Factory	Unlimited	100.00%	222,749,144.62	—2,054,657.54	—	14,773,325.38	—	(16,827,982.92)	117,310,759.19	103,383,727.89	220,694,487.08
Guangzhou Hanfang Modern Chinese Patent Medicine Research & Development Co., Ltd.	Unlimited	70.04%	68,198,509.35	—16,642,975.77	—	(16,642,975.77)	—	—	89,480,000.00	-37,924,466.42	51,555,533.58
Guangzhou Qixing Pharmaceutical Factory	Unlimited	100.00%	182,277,214.12	10,978,462.89	—	27,624,390.15	—	(16,645,927.26)	126,775,482.62	66,480,194.39	193,255,677.01
Guangzhou Jing Xiu Tang Pharmaceutical Co., Ltd.	Unlimited	88.40%	93,528,812.86	15,289,263.42	—	15,289,263.42	—	—	101,489,814.94	7,328,261.34	108,818,076.28
Guangzhou Pangaoshou Pharmaceutical Co., Ltd.	Unlimited	87.77%	160,065,937.53	10,924,705.38	—	14,983,120.20	—	(4,058,414.82)	144,298,132.51	26,692,510.40	170,990,642.91
Guangzhou Pharmaceuticals Corporation	Unlimited	90.09%	393,544,113.13	29,209,368.90	—	55,139,087.13	—	(25,929,718.23)	230,189,155.53	192,564,326.50	422,753,482.03
Guangzhou Chinese Medicine Corporation	Unlimited	100.00%	20,122,244.15	-856,949.67	—	(856,949.67)	—	—	74,378,883.83	(55,113,589.35)	19,265,294.48
Guangzhou Pharmaceutical Import & Export Corporation	Unlimited	100.00%	23,070,250.47	821,375.31	—	1,841,431.30	—	(1,020,055.99)	18,557,328.73	5,334,297.05	23,891,625.78



# NOTES TO THE FINANCIAL STATEMENTS

## VII. NOTES TO THE ACCOUNTS OF THE COMPANY (ALL AMOUNTS ARE STATED IN RMB YUAN UNLESS OTHERWISE STATED) (Continued)

### 3 Long-term equity investments (Continued)

#### (2) Equity investment to subsidiaries under equity method (Continued)

Name of the Investee	Term	% of Paid-in Capital of the Investee	Beginning Balance		Movement of Equity Interest in the Current Year				Closing Balance		Total
			Balance	Total of the Current Year	Investment Cost	Including Proceeds Recognized	Amortization of Difference	Profit Distribution	Initial Cost	Accumulated Movement	
Guangzhou Baidi Biotechnology Co., Ltd.	Unlimited	95.69%	57,906,132.27	(12,274,039.33)	—	(12,228,620.57)	(45,418.76)	—	80,000,000.00	(34,367,907.06)	45,632,092.94
Guangzhou Huanye Pharmaceutical Co., Ltd.	Unlimited	100.00%	15,184,066.54	9,605,601.93	9,599,194.01	218,321.32	(99,234.12)	(112,679.28)	24,930,440.77	(140,772.30)	24,789,668.47
Guangzhou Pharmaceutical Ying Bang Trading Co., Ltd.	Unlimited	51.00%	4,650,039.50	(408,035.44)	—	(316,863.01)	(91,172.43)	—	3,888,713.99	353,290.07	4,242,004.06
Guangxi Ying Kang Pharmaceutical Co., Ltd.	Unlimited	51.00%	16,800,080.16	136,941.73	—	202,563.37	(65,621.64)	—	21,717,000.00	(4,779,978.11)	16,937,021.89
<b>Total</b>			<b>1,797,763,513.33</b>	<b>124,961,850.94</b>	<b>46,413,594.01</b>	<b>205,264,582.84</b>	<b>(301,446.95)</b>	<b>(126,414,878.96)</b>	<b>1,351,361,752.61</b>	<b>571,363,611.66</b>	<b>1,922,725,364.27</b>



#### (3) Equity investment to joint ventures under equity method

Name of the Investee	Term	% of Paid-in Capital of the Investee	Beginning Balance		Movement of Equity Interest in the Current Year				Closing Balance		Total
			Balance	Total of the Current Year	Investment Cost	Including Proceeds Recognized	Amortization of Difference	Profit Distribution	Initial Cost	Accumulated Movement	
Guangzhou Wanglaoji Pharmaceutical Co., Ltd.	Unlimited	48.05%	167,311,020.90	13,049,546.97	—	31,719,137.28	—	(18,669,590.31)	102,035,124.44	78,325,443.43	180,360,567.87
Golden Eagle Asset Management Co., Ltd.	Unlimited	20.00%	9,757,693.31	(1,394,106.54)	—	(1,394,106.54)	—	—	20,000,000.00	(11,636,413.23)	8,363,586.77
Guangzhou Jihua Health Medical Equipment Co., Ltd.	Unlimited	24.00%	2,094,885.57	(29,104.90)	—	(29,104.90)	—	—	4,200,000.00	(2,134,219.33)	2,065,780.67
Guangzhou Jinshen Pharmaceutical Technology Co., Ltd.	Unlimited	38.25%	82,521.47	(28,518.31)	—	(28,518.31)	—	—	765,000.00	(710,996.84)	54,003.16
<b>Total</b>			<b>179,246,121.25</b>	<b>11,597,817.22</b>	<b>—</b>	<b>30,267,407.53</b>	<b>—</b>	<b>(18,669,590.31)</b>	<b>127,000,124.44</b>	<b>63,843,814.03</b>	<b>190,843,938.47</b>



# NOTES TO THE FINANCIAL STATEMENTS

## VII. NOTES TO THE ACCOUNTS OF THE COMPANY (ALL AMOUNTS ARE STATED IN RMB YUAN UNLESS OTHERWISE STATED) (Continued)

### 3 Long-term equity investments (Continued)

(4) Including: Equity investment differences

Name of the Investee	Initial Amount	Reason	Amortization Term	Current Amortization	Closing Balance
Guangzhou Baidi Biotechnology Co., Ltd.	454,187.62	Difference between payment for capital increment and attributable owners' equity	10 years	45,418.76	325,640.84
Guangzhou Huanye Pharmaceutical Co., Ltd.	992,341.19	Difference between payments for purchase of equity interest & capital increment, and attributable owners' equity	10 years	99,234.12	595,404.71
Guangzhou Pharmaceutical Ying Bang Trading Co., Ltd.	911,724.29	Difference between purchase payment of equity interest and attributable owners' equity	10 years	91,172.43	653,402.41
Guangxi Ying Kang Pharmaceutical Co., Ltd.	656,216.43	Difference between purchase payment of equity interest and attributable owners' equity	10 years	65,621.64	475,756.92
Total	<u>3,014,469.53</u>			<u>301,446.95</u>	<u>2,050,204.88</u>

### 4. Revenue from and cost of main operations

Item	Revenue from Main Operation		Cost of Main Operation	
	Current	Cumulated	Current	Cumulated
Wholesale	298,083,925.50	—	284,682,141.57	—
Retail	8,488,575.25	—	8,274,008.96	—
	<u>306,572,500.75</u>	<u>—</u>	<u>292,956,150.53</u>	<u>—</u>



# NOTES TO THE FINANCIAL STATEMENTS

## VII. NOTES TO THE ACCOUNTS OF THE COMPANY (ALL AMOUNTS ARE STATED IN RMB YUAN UNLESS OTHERWISE STATED) (Continued)

### 5 Investment income

#### (1) Current Year

Category	Proceeds on Fund Investment	Proceeds on Debenture Investment	Equity Investment Income Recognized under Cost Method	Equity Investment Income Recognized under Equity Method	Amortization of Equity Investment Differences	Provision for Impairment	Total
Short-term investment	4,976,837.00	18,238,626.34	—	—	—	1,048,000.00	24,263,463.34
Long-term equity investment	—	—	4,486,255.00	231,897,335.75	(301,446.95)	—	236,082,143.80
	<u>4,976,837.00</u>	<u>18,238,626.34</u>	<u>4,486,255.00</u>	<u>231,897,335.75</u>	<u>(301,446.95)</u>	<u>1,048,000.00</u>	<u>260,345,607.14</u>

#### (2) Last Year

Category	Proceeds on Debenture Investment	Equity Investment Income Recognized under Cost Method	Equity Investment Income Recognized under Equity Method	Amortization of Equity Investment Differences	Provision for Impairment	Total
Short-term investment	8,411,445.27	—	—	—	(7,659,480.00)	751,965.27
Long-term equity investment	—	3,383,850.00	198,070,654.32	(291,948.41)	—	201,162,555.91
Total	<u>8,411,445.27</u>	<u>3,383,850.00</u>	<u>198,070,654.32</u>	<u>(291,948.41)</u>	<u>(7,659,480.00)</u>	<u>201,914,521.18</u>

Proceeds on debenture investment mainly represent the net income from interest of entrusted loans received from the subsidiaries.



# NOTES TO THE FINANCIAL STATEMENTS

## VIII. RELATED PARTY RELATIONSHIPS AND TRANSACTIONS

### 1. Related parties with control relationship

#### A. Related parties with control relationship

Company name	Registered address	Principal business	Relation-ship with the Company	Economic nature and type	Legal representative
Guangzhou Pharmaceutical Holdings Limited	No. 45, Shamian North Street, Guangzhou	Production and sales	Holding	Company with limited liabilities	Yang Rongming
Guangzhou Xingqun Pharmaceutical Co., Ltd.	No. 162, Nanzhou Road, Guangzhou	Production and sales	Subsidiary	Joint stock company with limited liabilities	Su Guangfeng
Guangzhou Zhongyi Pharmaceutical Co., Ltd.	West Building of 11F, No. 28, Times Square, Tianhe North, Guangzhou	Production and sales	Subsidiary	Company with limited liabilities	Xu Jian
Guangzhou Chenlijj Pharmaceutical Factory	No. 1688, Guangzhou Avenue South, Guangzhou	Production and sales	Subsidiary	State-owned holding company	Ouyang Qiang
Guangzhou Qixing Pharmaceutical Factory	No. 33, Chigang North Street, Xingang Central Road, Guangzhou	Production and sales	Subsidiary	State-owned holding company	Wen Xinmin
Guangzhou Jing Xiu Tang Pharmaceutical Co., Ltd.	No. 179, Renmin South Road, Guangzhou	Production and sales	Subsidiary	Joint stock company with limited liabilities	Yan Zhibiao
Guangzhou Pangaoshou Pharmaceutical Co., Ltd.	Dongsheng Industry District Shigiao Guangzhou	Production and sales	Subsidiary	Joint stock company with limited liabilities	Wei Dahua
Guangzhou Pharmaceuticals Corporation	No.97, Datong Road, Guangzhou	Wholesale and retail	Subsidiary	Company with limited liabilities	Feng Zansheng
Guangzhou Chinese Medicine Corporation	No. 140, Guangfu South Road, Guangzhou	Wholesale and retail	Subsidiary	State-owned holding company	Zhou Lushan
Guangzhou Pharmaceutical Import & Export Corporation	No. 59, Shamian North Street, Guangzhou	Wholesale and retail	Subsidiary	State-owned holding company	Tu Kejin
Guangzhou Huanye Pharmaceutical Co., Ltd.	No. 195, Fangcun Avenue East, Fangcun District, Guangzhou	Production and sales	Subsidiary	Company with limited liabilities	Feng Jinglin
Guangzhou Hanfang Modern Chinese Patent Medicine Research & Development Co., Ltd.	No. 134, Jiangnan Avenue Central, Haizhu District, Guangzhou	Wholesale & retail, research & development	Subsidiary	Company with limited liabilities	Huang Jianjun
Guangzhou Baidi Biotechnology Co., Ltd.	Shiguang Roadside, Xiecun Village, Zhongcun Town, Panyu District, Guangzhou	Wholesale & retail, research & development	Subsidiary	Company with limited liabilities	Chen Jiannong



# NOTES TO THE FINANCIAL STATEMENTS

## VIII. RELATED PARTY RELATIONSHIPS AND TRANSACTIONS (Continued)

### 1. Related parties with control relationship (Continued)

#### A. Related parties with control relationship (Continued)

Company name	Registered address	Principal business	Relation-ship with the Company	Economic nature and type	Legal representative
Guangzhou Pharmaceutical Ying Bang Trading Co., Ltd.	Back building of 59 Shamian North Street, Guangzhou	Wholesale and retail	Subsidiary	Company with limited liabilities	He Shuhua
Guangxi Ying Kang Pharmaceutical Co., Ltd.	No. 193, Changgang Road, Nanning, Guangxi	Production and sales	Subsidiary	Company with limited liabilities	He Shuhua

#### B. Registered capital of related parties with control relationship and its change (Monetary unit: RMB'000)

Name of the Company	Beginning Balance	Current Increase	Current Decrease	Closing Balance
Guangzhou Pharmaceutical Holdings Limited	1,007,700	—	—	1,007,700
Guangzhou Xingqun Pharmaceutical Co., Ltd.	77,170	—	—	77,170
Guangzhou Zhongyi Pharmaceutical Co., Ltd.	166,000	—	—	166,000
Guangzhou Chenliji Pharmaceutical Factory	112,850	—	—	112,850
Guangzhou Qixing Pharmaceutical Factory	82,420	—	—	82,420
Guangzhou Jing Xiu Tang Pharmaceutical Co., Ltd.	86,230	—	—	86,230
Guangzhou Pangaoshou Pharmaceutical Co., Ltd.	65,440	—	—	65,440
Guangzhou Pharmaceuticals Corporation	222,000	—	—	222,000
Guangzhou Chinese Medicine Corporation	75,030	—	—	75,030
Guangzhou Pharmaceutical Import & Export Corporation	15,000	—	—	15,000
Guangzhou Huanye Pharmaceutical Co., Ltd.	6,000	—	—	6,000
Guangzhou Hanfang Modern Chinese Patent Medicine Research & Development Co., Ltd.	127,760	—	—	127,760
Guangzhou Baidi Biotechnology Co., Ltd.	83,600	—	—	83,600
Guangzhou Pharmaceutical Ying Bang Trading Co., Ltd.	18,410	—	—	18,410
Guangxi Ying Kang Pharmaceutical Co., Ltd.	31,880	—	—	31,880



# NOTES TO THE FINANCIAL STATEMENTS

## VIII. RELATED PARTY RELATIONSHIPS AND TRANSACTIONS *(Continued)*

### 1. Related parties with control relationship *(Continued)*

C. Shareholding held by related parties with control relationship and its change (Monetary unit: RMB'000)

Name of the Company	Beginning Balance		Current Increase		Current Decrease		Closing Balance	
	Amt.	%	Amt.	%	Amt.	%	Amt.	%
Guangzhou Pharmaceutical Holdings Limited	491,000	60.55	—	—	22,400	2.76	468,600	57.79
Guangzhou Xingqun Pharmaceutical Co., Ltd.	68,670	88.99	—	—	—	—	68,670	88.99
Guangzhou Zhongyi Pharmaceutical Co., Ltd.	150,000	90.36	16,000	9.64	—	—	166,000	100
Guangzhou Chenlijing Pharmaceutical Factory	112,850	100	—	—	—	—	112,850	100
Guangzhou Qixing Pharmaceutical Factory	82,420	100	—	—	—	—	82,420	100
Guangzhou Jing Xiu Tang Pharmaceutical Co., Ltd.	76,230	88.40	—	—	—	—	76,230	88.40
Guangzhou Pangaoshou Pharmaceutical Co., Ltd.	57,440	87.78	—	—	—	—	57,440	87.78
Guangzhou Pharmaceuticals Corporation	200,000	90.09	—	—	—	—	200,000	90.09
Guangzhou Chinese Medicine Corporation	7,5030	100	—	—	—	—	75,030	100
Guangzhou Pharmaceutical Import & Export Corporation*	15,000	100	—	—	—	—	15,000	100
Guangzhou Huanye Pharmaceutical Co., Ltd.	3,580	59.70	242	40.30	—	—	6,000	100
Guangzhou Hanfang Modern Chinese Patent Medicine Research & Development Co., Ltd.	89,480	70.04	—	—	—	—	89,480	70.04
Guangzhou Baidi Biotechnology Co., Ltd.	80,000	95.69	—	—	—	—	80,000	95.69
Guangzhou Pharmaceutical Ying Bang Trading Co., Ltd.	9,388	51.00	—	—	—	—	9,388	51.00
Guangxi Ying Kang Pharmaceutical Co., Ltd.	16,260	51.00	—	—	—	—	16,260	51.00



# NOTES TO THE FINANCIAL STATEMENTS

## VIII. RELATED PARTY RELATIONSHIPS AND TRANSACTIONS (Continued)

### 1. Related parties with control relationship (Continued)

#### D. Related parties with joint control relationship

Company name	Registered address	Principal business	Relationship with the Company	Economic nature and type	Legal representative
Guangzhou Wanglaoji Pharmaceutical Co., Ltd.	Jiangcun Bridge side, Baiyun District, Guangzhou	Production and sales	Cooperatively run enterprise	Joint stock company with limited liabilities	Li Zuze
Guangzhou Lianjie Computer Technology Co., Ltd.	7/F., 82, Shangjiu Rd., Guangzhou	Development and service of softwares	Cooperatively run enterprise	Company with limited liability	Tan Liqing
Guangzhou Pharmaceutical Football Club Co., Ltd.	45, Shamian North Road, Liwan District, Guangzhou	Sports and advertisement	Cooperatively run enterprise	Company with limited liability	Yang Rongming
Guangzhou Nuocheng Bio-product Cp. Ltd	Shijiang Roadside, Xjecun Village, Zhongcun Tawn Panyu District, Guangzhou	Production and Sales	Cooperatively run enterprise	Joint stock Company with limited liability	Chen Jionnong

#### E. Registered capital (paid-in capital) of related parties with joint control relationship and its change

Monetary unit: RMB '000

Name of the Company	Beginning Balance	Current Increase	Current Decrease	Closing Balance
Guangzhou Wanglaoji Pharmaceutical Co., Ltd.	204,760	—	—	204,760
Guangzhou Lianjie Computer Technology Co., Ltd.	500	—	—	500
Guangzhou Pharmaceutical Football Club Co., Ltd.	—	20,000	—	20,000
Guangzhou Nuocheng Bio-product Co., Ltd.	—	32,000	—	32,000



# NOTES TO THE FINANCIAL STATEMENTS

## VIII. RELATED PARTY RELATIONSHIPS AND TRANSACTIONS (Continued)

### 1. Related parties with control relationship (Continued)

F. Shareholding held by related parties with joint control relationship and its change

Monetary unit: RMB '000

Name of the Company	Beginning Balance		Current Increase		Current Decrease		Closing Balance	
	Amount	%	Amount	%	Amount	%	Amount	%
Guangzhou Wanglaoji Pharmaceutical Co., Ltd.	98,380	48.0465	—	—	—	—	98,380	48.0465
Guangzhou Lianjie Computer Technology Co., Ltd.	250	50	—	—	—	—	250	50
Guangzhou Pharmaceutical Football Club Co., Ltd.	—	—	9,220	46.10	—	—	9,220	46.10
Guangzhou Nuocheng Bio-product Co., Ltd.	—	—	16,000	50	—	—	16,000	50

### 2. Related parties with no control relationship

Name of the Company	Relationship with the Company
Guangzhou Baiyunshan Qiaoguang Pharmaceutical Co., Ltd.	Fellow subsidiary
Guangzhou Baiyunshan Mingxing Pharmaceutical Co., Ltd.	Fellow subsidiary
Guangzhou Baiyunshan Tianxin Pharmaceutical Co., Ltd.	Fellow subsidiary
Guangzhou Baiyunshan Hejigong Pharmaceutical Co., Ltd.	Fellow subsidiary
Guangzhou Baiyunshan Guanghua Pharmaceutical Co., Ltd.	Fellow subsidiary
Hutchison Whampoa Guangzhou Baiyunshan Chinese Medicine Company Limited	Fellow subsidiary
Guangzhou South-china Medical Appliance Co., Ltd.	Fellow subsidiary
Po Lian Development Co., Ltd.	Fellow subsidiary
Guangzhou Medicine Research Institute	Fellow subsidiary
Guangzhou Pharmaceutical Real Estate Industrial Co., Ltd.	Fellow subsidiary
Guangzhou Baiyunshan Chinese Medicine Factory	Fellow subsidiary
Guangzhou Baiyunshan Pharmaceutical Factory	Fellow subsidiary
Guangzhou Baiyunshan Chemistry Medicine Factory	Fellow subsidiary
Guangzhou Baiyunshan External Use Medicine Factory	Fellow subsidiary
Guangzhou Pharmaceutical Goods and Supply Company	Fellow subsidiary
Guangzhou Pharmaceutical Economic Development Company	Fellow subsidiary
Guangzhou Wanglaoji Pharmaceutical Co., Ltd.	Joint venture
Guangzhou Lianjie Computer Technology Co., Ltd.	Joint venture
Guangzhou Pharmaceutical Football Club Co., Ltd.	Joint Venture



# NOTES TO THE FINANCIAL STATEMENTS

## VIII. RELATED PARTY RELATIONSHIPS AND TRANSACTIONS *(Continued)*

### 3. Related Party Transactions *(Continued)*

- A. Transactions among the consolidated subsidiaries with control relationship as well as those between the Company and its subsidiaries have been eliminated.
- B. Purchase of goods
- a. Amount of the Transactions

*Monetary unit: RMB '000*

Name of the Company	2006	2005
Guangzhou Baiyunshan Qiaoguang Pharmaceutical Co., Ltd.	13,336	40,260
Guangzhou Baiyunshan Mingxing Pharmaceutical Co., Ltd.	33,003	38,479
Guangzhou Baiyunshan Tianxin Pharmaceutical Co., Ltd.	45,411	37,468
Guangzhou Baiyunshan Hejigong Pharmaceutical Co., Ltd.	37,725	10,113
Guangzhou Baiyunshan Guanghua Pharmaceutical Co., Ltd.	74,093	69,722
Guangzhou South-china Medical Appliance Co., Ltd.	33	6
Guangzhou Pharmaceutical Real Estate Industrial Co., Ltd.	3	—
Po Lian Development Co., Ltd.	232,899	160,840
Hutchison Whampoa Guangzhou Baiyunshan Chinese Medicine Company Limited	52,769	39,950
Guangzhou Baiyunshan Pharmaceutical Factory	52,057	52,135
Guangzhou Baiyunshan Chemistry Medicine Factory	7,606	2,295
Guangzhou Baiyunshan External Use Medicine Factory	7,012	5,578
Guangzhou Pharmaceutical Economic Development Company	12	15
Guangzhou Pharmaceutical Goods and Supply Company	3	—
Guangzhou Wanglaoji Pharmaceutical Co., Ltd.	96,605	26,310
	<b>652,567</b>	<b>483,171</b>

- b. The abovementioned purchases are settled at the price as regulated by the government or its pricing regulations.





# NOTES TO THE FINANCIAL STATEMENTS

## VIII. RELATED PARTY RELATIONSHIPS AND TRANSACTIONS (Continued)

### 3. Related Party Transactions (Continued)

#### C. Sales of goods

##### a. Amount of the Transactions

Monetary unit: RMB '000

Name of the Company	2006	2005
Guangzhou Baiyunshan Qiaoguang Pharmaceutical Co., Ltd.	59,487	61,207
Guangzhou Baiyunshan Mingxing Pharmaceutical Co., Ltd.	18,265	13,227
Guangzhou Baiyunshan Tianxin Pharmaceutical Co., Ltd.	11,181	18,143
Guangzhou Baiyunshan Hejigong Pharmaceutical Co., Ltd.	3,967	1,487
Guangzhou Baiyunshan Guanghua Pharmaceutical Co., Ltd.	49,965	42,878
Guangzhou Medicine Research Institute	7	2
Guangzhou Wanglaoji Pharmaceutical Co., Ltd.	40,194	20,700
Hutchison Whampoa Guangzhou Baiyunshan Chinese Medicine Company Limited	11,459	17,715
Guangzhou Baiyunshan Pharmaceutical Factory	26,513	24,443
Guangzhou Baiyunshan Chemistry Medicine Factory	13,729	20,430
Guangzhou Baiyunshan External Use Medicine Factory	2,191	1,763
Guangzhou Pharmaceutical Economic Development Company	22	—
	<u>236,980</u>	<u>221,995</u>

b. The abovementioned sales are settled at the price as regulated by the government or its pricing regulations.

#### D. Receivables and payables

Monetary unit: RMB '000

Item	Closing Balance	Beginning Balance
<b>Accounts receivable:</b>		
Guangzhou Baiyunshan Qiaoguang Pharmaceutical Co., Ltd.	34,767	26,468
Guangzhou Baiyunshan Mingxing Pharmaceutical Co., Ltd.	1,081	1,714
Guangzhou Baiyunshan Tianxin Pharmaceutical Co., Ltd.	1,413	1,842
Guangzhou Baiyunshan Hejigong Pharmaceutical Co., Ltd.	701	238
Guangzhou Baiyunshan Guanghua Pharmaceutical Co., Ltd.	6,901	2,895
Guangzhou Wanglaoji Pharmaceutical Co., Ltd.	509	2,268
Hutchison Whampoa Guangzhou Baiyunshan Chinese Medicine Company Limited	693	1,777
Guangzhou Baiyunshan Pharmaceutical Factory	3,919	4,224
Guangzhou Baiyunshan Chemistry Medicine Factory	3,267	1,208
Guangzhou Baiyunshan External Use Medicine Factory	858	170
Guangzhou Pharmaceutical Economic Development Company	26	—



# NOTES TO THE FINANCIAL STATEMENTS

## VIII. RELATED PARTY RELATIONSHIPS AND TRANSACTIONS (Continued)

### 3. Related Party Transactions (Continued)

#### D. Receivables and payables (Continued)

Monetary unit: RMB '000

Item	Closing Balance	Beginning Balance
<b>Accounts payable:</b>		
Guangzhou Baiyunshan Qiaoguang Pharmaceutical Co., Ltd.	19	1,632
Guangzhou Baiyunshan Mingxing Pharmaceutical Co., Ltd.	131	2,293
Guangzhou Baiyunshan Tianxin Pharmaceutical Co., Ltd.	45	206
Guangzhou Baiyunshan Hejigong Pharmaceutical Co., Ltd.	—	524
Guangzhou Baiyunshan Guanghua Pharmaceutical Co., Ltd.	8,477	740
Guangzhou South-china Medical Appliance Co., Ltd.	23	11
Po Lian Development Co., Ltd.	28,229	49,750
Guangzhou Baiyunshan Pharmaceutical Factory	65	10
Guangzhou Baiyunshan Chemistry Medicine Factory	702	—
Guangzhou Baiyunshan External Use Medicine Factory	421	292
Hutchison Whampoa Guangzhou Baiyunshan Chinese Medicine Company Limited	—	2,046
Guangzhou Pharmaceutical Economic Development Company	15	17
Guangzhou Wanglaoji Pharmaceutical Co., Ltd.	3,393	148
Guangzhou Pharmaceutical Goods and Supply Company	2	—
Guangzhou Pharmaceutical Real Estate Industrial Co., Ltd.	3	—
<b>Other receivables:</b>		
Guangzhou Pharmaceutical Holdings Limited	4,071	5,060
Guangzhou South-china Medical Appliance Co., Ltd.	100	100
Po Lian Development Co., Ltd.	—	7,993
Guangzhou Lianjie Computer Technology Co., Ltd.	—	520
Guangzhou Wanglaoji Pharmaceutical Co., Ltd.	362	—
<b>Other payables:</b>		
Guangzhou Pharmaceutical Holdings Limited	16,994	25,468
Po Lian Development Co., Ltd.	82	—
Guangzhou Zhongfu Medical Co., Ltd.	—	1,235
Guangzhou Wanglaoji Pharmaceutical Co., Ltd.	97	97
Guangzhou Pharmaceutical Goods and Supply Company	3,000	3,000
Guangzhou Pharmaceutical Football Club Co., Ltd.	100	—
<b>Advances to suppliers:</b>		
Hutchison Whampoa Guangzhou Baiyunshan Chinese Medicine Company Limited	345	197
Guangzhou Baiyunshan Mingxing Pharmaceutical Co., Ltd.	8,376	—
Guangzhou Baiyunshan Tianxin Pharmaceutical Co., Ltd.	1,543	—
Guangzhou Baiyunshan Hejigong Pharmaceutical Co., Ltd.	129	—
Guangzhou Baiyunshan Guanghua Pharmaceutical Co., Ltd.	8,748	—
Po Lian Development Co., Ltd.	9,369	—
<b>Advances from customers:</b>		
Guangzhou Baiyunshan Qiaoguang Pharmaceutical Co., Ltd.	—	22
Guangzhou Baiyunshan Mingxing Pharmaceutical Co., Ltd.	—	279
Guangzhou Baiyunshan Hejigong Pharmaceutical Co., Ltd.	—	91
Guangzhou Baiyunshan Guanghua Pharmaceutical Co., Ltd.	251	1
Hutchison Whampoa Guangzhou Baiyunshan Chinese Medicine Company Limited	—	300
Guangzhou Wanglaoji Pharmaceutical Co., Ltd.	—	176
Guangzhou Baiyunshan Pharmaceutical Factory	437	—



# NOTES TO THE FINANCIAL STATEMENTS

## VIII. RELATED PARTY RELATIONSHIPS AND TRANSACTIONS *(Continued)*

### 3. Related Party Transactions *(Continued)*

#### E. Receipt of services

*Monetary unit: RMB '000*

Item	Note	2006	2005
Service fee on staff quarters	1	274	310
Comprehensive service fee	2	939	860
Advertisement and promotion provided by Guangzhou Pharmaceutical Football Club Co., Ltd.	3	19,144	—
		<u>20,357</u>	<u>1,170</u>

*Note 1: Pursuant to the Accommodation Service Agreement entered into by the Group and the Holding on September 1, 1997 and supplementary on December 31, 1997, the Holding agreed to provide employees of the Group continuously staff quarters. The Group agreed to pay a service fee equals to 6% of the net book value of the relevant staff quarters. The Accommodation Services Agreement will be expired on December 31, 2007.*

*Note 2: Pursuant to the Composite Services Agreement established by the Group and the Holding on September 1, 1997, the Holding agreed to provide certain welfare facilities to the Group. The Group agreed to be responsible for the operation, management and maintenance of the facilities and pay a welfare facilities fee equals to the Holding's total depreciation charges of the welfare facilities in the year ended December 31, 1997 plus a 10% annual increment based on the welfare facilities for the previous year. The Composite Service Agreement will be expired on December 31, 2007.*

*Note 3: Pursuant to the Agreement on Related Party Transactions of Continuous Advertisement entered into by the Group and Guangzhou Pharmaceutical Football Club Co., Ltd. on June 15, 2006, Guangzhou Pharmaceutical Football Club Co., Ltd. promotes the brand and the products of the Group as well as provides advertisement by its own football team and matches undertaken. The transaction of advertisement is priced at fair benchmark price through negotiation and the total amount of transactions per year is no more than HKD 30,000 thousand within the period from March 1, 2006 to December 31, 2008. This agreement will be expired on December 31, 2008.*

#### F. Rental

Pursuant to the Tenancy Agreement and the Office Building Tenancy Agreement both entered into by the Group and the Holding on September 1, 1997, the Holding granted to the Group the right to use certain premises as warehouses and offices, in which the term of the Office Building Tenancy Agreement was 3 years, and the agreement will be renewed when expired, the rental was paid at a fixed annual amount which were subject to the adjustment of standard rental as prescribed from time to time by Guangzhou Real Estate Administration Bureau; the tenancy agreements for other properties will be expired on September 1, 2007 at rentals which were determined by the utilities and other outgoings which were payable based on the actual consumption.

According to the Office Building Tenancy Agreement established by the Group and the Holding on February 6, 2004, the Group rented the back tower of the Holding's building at No. 45 Shamian North Street at a fixed annual rent which was subject to the adjustment of standard rental as prescribed from time to time by Guangzhou Real Estate Administration Bureau, the term will be expired until the rental prepayment is fully offset.

The Group should pay such rental charges of RMB 2,944 thousand for the current year (last cumulated: RMB 3,450 thousand).



# NOTES TO THE FINANCIAL STATEMENTS

## VIII. RELATED PARTY RELATIONSHIPS AND TRANSACTIONS *(Continued)*

### 3. Related Party Transactions *(Continued)*

#### G. License fee

Pursuant to the Trademark License Agreement entered into by the Group and the Holding on September 1, 1997, the Holding granted the Group an exclusive right to use 38 trademarks owned by the Holding for a term of 10 years commencing at the signature date. The Group agreed to pay license fees for the use of the trademarks at 0.1% of its aggregate net sales. The Trademark License Agreement will be expired on September 1, 2007. The Group should pay the above license fee of RMB 10,782 thousand for the current year (last cumulated: RMB 12,230 thousand).

Pursuant to the Supplementary Agreement on Payment of Trademark License Using Fee dated July 28, 2005 signed by the Group, the Holding and Guangzhou Wanglaoji Pharmaceutical Co., Ltd., upon being changed to a foreign-invested enterprise, Guangzhou Wanglaoji Pharmaceutical Co., Ltd. Shall pay to the Holding at 2.1% of the net sales revenue as the Trademark License Using Fee, in which 53% shall be paid directly to the Holding and 47% to the Group. Up to the reporting period, the Group should collect the abovementioned trademark license using fee with the amount of RMB 9,736 thousand from Guangzhou Wanglaoji Pharmaceutical Co., Ltd..

#### H. Prepaid rental

In accordance with the Premises Agreement entered into by the Group and the Holding on August 28, 1998, the Holding agreed to grant the Group the right to use certain units of its new office building. The rent paid by the Group was determined by reference to a 38% discount on the market rent when the formal tenancy agreement was signed. As the Holding required funds for constructing the new office building, the Group made an advance payment of RMB 6,000 thousand to the Holding during the year as agreed in the aforementioned agreement. The Holding has consented to use the advance payment exclusively for the construction of the new office building and offset the rental for the premises owed by the Group. The term will be expired until the advance payment is fully offset. The Group has prepaid such rental charges of RMB 3,792 thousand by December 31, 2006.



# NOTES TO THE FINANCIAL STATEMENTS

## IX. CONTINGENT EVENTS

### 1. The Group

Up to December 31, 2006, there are no guaranties for external companies.

### 2. The Company

As at December 31, 2006, the Company has provided guaranties for the following subsidiaries:

*Monetary unit: RMB '000*

Company guaranteed	Guaranty content	Amount	Period
Guangzhou Pharmaceuticals Corporation	Loan of working capital	220,000	1 year
Guangzhou Chinese Medicine Corporation	Loan of working capital	10,000	1 year
Guangzhou Pharmaceutical Imp. & Exp. Corporation	Loan of working capital	10,000	1 year
Guangzhou Hanfang Modern Chinese Patent Medicine Research & Development Co., Ltd.	Loan of Working capital	34,920	1 year
Guangzhou Baidi Biotechnology Co., Ltd.	Loan of Working capital	10,000	1 year
Guangzhou Pharmaceuticals Corporation	Bill	60,630	1 year
Guangzhou Pharmaceutical Imp. & Exp. Corporation	Bill and Trading quota	18,530	1 year
Total		<u>364,080</u>	



## X. COMMITMENTS

1. Up to December 31, 2006, material commitments of the Group are as follows:

*Monetary unit: RMB '000*

	Closing Balance	Beginning Balance
Project and equipment payables with contract signed	<b>12,677</b>	61,448
Rental payables with contract signed	<b>90,738</b>	84,928

2. Up to December 31, 2006, Guangzhou Pangaoshou Pharmaceutical Co., Ltd., the subsidiary of the Group, has mortgaged its plant with the net value of 54,970 thousand at Dongsheng Industry District of Shiqiao for a bank loan of RMB 30,000 thousand for working capital; Guangzhou Pharmaceuticals Corporation, another subsidiary of the Group, has discounted its undue trade acceptance bill with the amount of RMB 139,613 thousand for a loan by pledge.

# NOTES TO THE FINANCIAL STATEMENTS

## XI. NON-ADJUSTING EVENTS OCCURRING AFTER THE BALANCE SHEET DATE

1. On January 10, 2007, the Equity Transfer Contract was signed by the Company, the Holding, Anhui Huadong Chinese Medicine Engineering Group Limited and five natural persons e.g. Liu Juyan, etc.. Pursuant to the contract, the Company will acquire the equity interest totaling up to 26.04% of the subsidiary, Guangzhou Hanfang Modern Chinese Patent Medicine Research & Development Co., Ltd. (hereinafter referred to as "Hanfang"), from the abovementioned parties at the total consideration of RMB 23,299,010.

On January 10, 2007, Hanfang signed the Merger Agreement with the wholly owned subsidiary of the Company, Guangzhou Huanye Pharmaceutical Co., Ltd. (hereinafter referred to as "Huanye"). Pursuant to the agreement, both parties agree that Hanfang will merge with Huanye by absorption of all business, assets and liabilities of Huanye. Upon the merger, Hanfang will exist while Huanye will be deregistered.

2. On January 27, 2007, the Transfer Contract on Contribution of Guangzhou Pharmaceuticals Corporation was signed by Guangzhou Jing Xiu Tang Pharmaceutical Co., Ltd., Guangzhou Pangaoshou Pharmaceutical Co., Ltd. (both are the holding subsidiaries of the Company), and 33 natural persons with Alliance BMP Ltd., which is subordinated to Alliance Boots Plc.. Pursuant to the transfer contract, Alliance BMP Ltd. will acquire the equity interest in Guangzhou Pharmaceuticals Corporation at the percentage of 3.919%, 3.919% and 2.072% held by Guangzhou Jing Xiu Tang Pharmaceutical Co., Ltd., Guangzhou Pangaoshou Pharmaceutical Co., Ltd. and 33 natural persons at the consideration of RMB 23,709,950, RMB 23,709,950 and RMB 12,535,600 respectively. The relevant contract is to be approved by the Ministry of Commerce of P.R. China.

On January 27, 2007, the Capital Increment Contract of Guangzhou Pharmaceuticals Corporation was signed by the Company with Alliance BMP Ltd.. Pursuant to the contract, Alliance BMP Ltd. will solely increase its contribution upon acquiring 9.91% of the equity interest of Guangzhou Pharmaceuticals Corporation from Guangzhou Jing Xiu Tang Pharmaceutical Co., Ltd., Guangzhou Pangaoshou Pharmaceutical Co., Ltd. and 33 natural persons. After the increment, both the Company and Alliance BMP Ltd. will hold 50% of the equity interest of Guangzhou Pharmaceuticals Corporation. Alliance BMP Ltd. will make contribution at RMB 485,089,000 in foreign currency. The relevant contract is to be approved by the Ministry of Commerce of P.R. China.

3. On January 27, 2007, the Company purchased the property located at No. 82, Shangjiu Road and formerly owned by Guangzhou Pharmaceuticals Corporation, the holding subsidiary of the Company, at the price of RMB 41,116,178. The procedure of ownership transfer was fulfilled on March 29, 2007.



# NOTES TO THE FINANCIAL STATEMENTS

## XI. NON-ADJUSTING EVENTS OCCURRING AFTER THE BALANCE SHEET DATE

(continued)

4. In year 2001, the Holding pledged its holding shares of the Company for debt restructuring of Guangzhou Baiyunshan Pharmaceutical Co., Ltd., including: mortgaging 65.11 million shares to entities like Guangzhou Beicheng Rural Credit Cooperative (hereinafter referred to as "Beicheng RCC"), etc.. Pursuant to the Civil Ruling Documents with reference (2005) SZFZZ No. 689, 736-744, 779, 780 and 847 issued by the Intermediate People's Court of Guangzhou, Guangdong Province on May 8, 2006, the ownership of the abovementioned shares should be transferred to the institutions like Beicheng RCC, etc., but the relevant procedure for transferring ownership had not been fulfilled at that time. 4.22 million and 3.48 million shares of the Company with limit on sales, which were pledged to Guangzhou Xinjiao Rural Credit Cooperative and Guangzhou Xinfeng Rural Credit Cooperative respectively by the Holding, have been transferred to these rural credit cooperatives respectively and the registration procedures were fulfilled in February 2007. On March 23, 2007, the Holding changed the ownership of the pledged 46.67 million shares and 1.72 million shares of the Company with limit on sales to Beicheng RCC and Guangzhou Baiyun Rural Credit Cooperative respectively. Thus, the holding equity interest of the Company of the Holding drops from 57.79% to 50.87%, while Beicheng RCC increases its holding equity interest of the Company from 0.00% to 5.76%. The procedure for transferring ownership of the 9.02 million shares ruled to be transferred to Guangzhou Huangshi Rural Credit Cooperative has not yet fulfilled.
5. As suggested by the Board of Directors, the dividend allocation plan for the year 2006 will be: the Company proposes to allocate RMB0.084 per share, therefore the total dividends to be allocated are RMB68,115,600 at the total shares of 810,900,000.
6. On 16 March 2007, the National People's Congress approved the Enterprise Income Tax Law of PRC (the "new EIT Law"), which will be effective from 1 January 2008.

Since the deferred tax assets and deferred tax liabilities shall be measured at the tax rates that are expected to apply to the period when the asset is realized or the liability is settled, the change in the applicable tax rate will affect the determination of the carrying values of deferred tax assets and deferred tax liabilities of the Group. As at the date that these financial statements are approved for issue, detailed measures of the new EIT Law have not been issued yet. The Group could not estimate the impact to itself as implementing the new EIT Law, due to the indefinite detailed stipulations concerning the following items of the period after 2008, such as: applicable tax rate, computation of taxable income, specific preferential tax treatments and their related transitional measures. The Group will further evaluate the impact to its operating results and financial positions of future periods as more aforesaid detailed measures and other related regulations are announced.

## XII. OTHER EVENTS

During the current reporting period, there are no debt restructuring events in the Group.

During the current reporting period, there are no material non-monetary transactions in the Group.



# NOTES TO THE FINANCIAL STATEMENTS

## XIII. EXTRAORDINARY GAINS AND LOSSES IN THE CURRENT YEAR

	2006	2005
Gains and losses on disposal of long-term equity investment	<b>(2,455,034.47)</b>	(805,506.27)
Government subsidies of all kinds	<b>1,190,244.21</b>	720,456.65
Short-term investment gains or losses	<b>6,024,837.00</b>	(7,659,480.00)
Other non-operating expenditures after deducting the accrued provision for impairment of assets	<b>(2,213,974.62)</b>	1,052,367.46
Gains or losses on entrusted investment	<b>(1,099,045.72)</b>	(517,355.66)
Reversal of provisions for impairment accrued in the previous years	—	6,642,181.93
Impact on the income tax	<b>(591,319.20)</b>	(553,380.03)
Impact on the gain or loss of minority shareholders	<b>(94,898.20)</b>	40,798.26
	<b><u>760,809.00</u></b>	<b><u>(1,079,917.66)</u></b>

## XIV. COMPARISON WITH THE DATA OF LAST YEAR

For the convenience of comparison with the data of last year, some items of last year's data in the notes to the financial statements are reclassified.

## XV. ANALYSIS ON THE MOVEMENT OF ACCOUNTING DATA

As at December 31, 2006 and December 31, 2005, items in the consolidated balance sheet moved with a range over 30%, and such items occupied more than 5% of the net assets of the Group as at December 31, 2006 additionally; items in the consolidated income statement moved with a range over 30%, and such items occupied more than 10% of the total profit of the Group for the year 2006 are as follows:

*Monetary unit: RMB '000*

Item	As at Dec. 31, 2006	As at Dec. 31, 2005	Movement	
			Amount	Range (%)
Accounts receivable (Note 1)	<b>1,401,804</b>	1,004,658	397,146	39.53
Statutory public welfare fund (Note 2)	—	179,462	(179,462)	(100)
Item	For the year 2006	For the year 2005	Amount	Range(%)
Net cash flows from financing activities (Note 3)	<b>(110,619)</b>	(291,930)	181,311	62.11

*Note 1: Compared with the beginning balance, the closing balance of accounts receivable increases by 39.53%, for the reason that in the current year, sales grows continuously as the Group keeps expanding its market and prolongs credit term of certain customers for higher market share.*

*Note 2: Compared with the beginning balance, the closing balance of statutory public welfare fund decreases by 100% in the current year, mainly because pursuant to the new Corporation Law and the document with reference CQ[2006]No.67, companies should manage and use the balance of statutory public welfare fund as at December 31, 2005 as surplus reserve. The Group has transferred the balance of statutory public welfare fund into statutory surplus reserve.*

*Note 3: Net cash flows from financing activities increases by 62.11% as compared with that of last year, mainly because that the net repayment to the bank loans by the Group during the current year is RMB 264,350 thousand less than that of last year.*





# NOTES TO THE FINANCIAL STATEMENTS

## XVI. APPROVAL OF FINANCIAL STATEMENTS

The financial statements were approved by the board of directors and authorized for issuance on April 27, 2007.

## XVII. DIFFERENCES BETWEEN THE FINANCIAL STATEMENTS PREPARED IN ACCORDANCE WITH PRC ACCOUNTING STANDARDS AND SYSTEMS AND HKFRS

	Notes	At 31 December 2006 RMB'000	At 31 December 2005 RMB'000
Net assets under PRC Accounting Standards and Systems		<b>2,788,088</b>	2,621,437
Intangible assets capitalised	1	<b>27,006</b>	37,367
Difference arising from fixed assets revaluation	2	<b>126,547</b>	128,522
Deferred government grants	3	<b>(3,279)</b>	(4,259)
Difference in provision for employee benefits in medical insurance	4	<b>(60,197)</b>	(53,586)
Provision for deferred taxation	5	<b>23,082</b>	10,822
Impairment on goodwill	6	<b>(1,579)</b>	(1,791)
Revaluation of investment properties	7	<b>13,105</b>	—
Difference in minority interest	8	<b>(15,384)</b>	(15,389)
Capital and reserves attributable to equity holders of the Company under HKFRS		<b>2,897,389</b>	<b>2,723,123</b>
Net profit under PRC Accounting Standards and Systems		<b>227,328</b>	184,482
Amortisation of intangible assets	1	<b>(10,361)</b>	(10,382)
Additional depreciation on revalued fixed assets	2	<b>(1,975)</b>	(1,975)
Government grants recognised as income	3	<b>1,106</b>	452
Difference in provision for employee benefits in medical insurance	4	<b>(6,611)</b>	6,017
Provision for deferred taxation	5	<b>12,260</b>	4,841
Reversals of amortisation on goodwill/(Impairment on goodwill)	6	<b>212</b>	(1,791)
Unsettled long outstanding payables written off recognised as income	9	<b>2,498</b>	2,397
Negative goodwill arising from the additional investment of an external investor in a subsidiary	10	—	19,819
Negative goodwill arising from investment in an associate	11	<b>238</b>	—
Donations recognised as income	12	<b>91</b>	440
Appropriation to staff bonus and welfare fund charged as expenses	13	<b>(7,680)</b>	(6,074)
Decline in fair value of investment properties	14	<b>(12)</b>	—
Gain from disposals of fixed assets as recognised income	15	<b>729</b>	—
Difference in minority interests	8	<b>244</b>	(422)
Profit attributable to equity holders of the Company under HKFRS		<b>218,067</b>	<b>197,804</b>



# NOTES TO THE FINANCIAL STATEMENTS

## XVII. DIFFERENCES BETWEEN THE FINANCIAL STATEMENTS PREPARED IN ACCORDANCE WITH PRC ACCOUNTING STANDARDS AND SYSTEMS AND HKFRS (Continued)

1. This is an amortisation of staff quarter reform costs incurred by the Company and its subsidiaries (collectively the "Group") prior to 2000 in relation to purchases of staff quarters by its employees. Under HKFRS, such cost are recognised as an intangible asset and are subject to amortisation on a straight-line basis over a period of 10 years to reflect the estimated remaining average service life of its employees in which the related economic benefits are recognised. Under PRC Accounting Standards and Systems, the staff quarter reform costs were written off against retained earnings of the year in which they were incurred.
2. The Group's fixed assets were revalued by the international valuers in 1997 for the purpose of listing the Company's H shares. The revaluation has been reflected in the financial statements of the Group prepared under HKFRS but not in the financial statements prepared under PRC Accounting Standards and Systems. Accordingly, the depreciation charge under HKFRS is higher than that calculated under PRC Accounting Standards and Systems as the depreciation charge under HKFRS is based on the revalued amount of fixed assets.
3. Government subsidies allocated for fixed assets are recognised as capital reserve in the financial statements prepared in accordance with PRC Accounting Standards and Systems. Under HKFRS, government subsidies are recognised as deferred income and credited to the income statement on a straight line basis in accordance with the estimated useful lives of the assets.
4. On 1 December 2001, the Group has participated in a medical insurance scheme set up and managed by the Guangzhou People's Municipal Government as required by the Provisional Rules of Medical Insurance issued by the Guangzhou People's Municipal Government. Medical insurance relating to contributions accrued for the past service rendered by the retired and retiring employees are recognised as expenses in prior years under HKFRS. However, in the financial statements prepared under PRC Accounting Standards and Systems, medical insurance for the past service is recognised as expenses on cash basis. Cash basis is not acceptable under HKFRS.
5. The Group has not made provision for deferred tax in the financial statements prepared in accordance with PRC Accounting Standards and Systems. Under HKFRS, deferred tax is accounted for using the balance sheet liability method on all taxable temporary differences for deferred tax liability, and to recognise deferred tax assets to the extent that it is probable that taxable profits will be available against which deductible temporary differences can be utilised.
6. Goodwill is amortised using the straight-line method under PRC Accounting Standards and Systems. Under HKFRS, any impairment on goodwill is accounted for in the income statement on a yearly basis.
7. The properties leased out are classified as "Investment Properties" under HKFRS, and restated every year to their fair values. The amount represents the fair value gain recognised this year upon revaluation.
8. Due to the above adjustments, there is a difference in net profit / profit attributable to equity holders of the Company prepared under PRC Accounting Standards and Systems and HKFRS. This results in a difference in the minority interest.
9. Write-off of payable was recognised as capital reserve in the financial statements prepared in accordance with PRC Accounting Standards and Systems. Under HKFRS, it was recognised in the income statement and was transferred from profit after tax to capital reserve.



# NOTES TO THE FINANCIAL STATEMENTS

## XVII. DIFFERENCES BETWEEN THE FINANCIAL STATEMENTS PREPARED IN ACCORDANCE WITH PRC ACCOUNTING STANDARDS AND SYSTEMS AND HKFRS *(Continued)*

10. Equity in a subsidiary of the Company was diluted due to the issue of new shares to a third party by such subsidiary. Surplus arising from such transaction is recognised as capital reserve in the accounts prepared in accordance with PRC Accounting Standards and Systems. Under HKFRS, it is accounted for in the income statement.
11. A subsidiary of the Company invested into an associate, and the excess of the fair value of the Group's share of the net assets of the associate over the net book value of the assets injected was recognised as negative goodwill. Such goodwill was recognised in the income statement prepared in accordance with HKFRS.
12. Non-cash donation accepted by the Group was recognised as capital reserve in the financial statements prepared in accordance with PRC Accounting Standards and Systems. Under HKFRS, it was recognised in the income statement and was transferred from profit after tax to capital reserve.
13. This was the staff bonus and welfare fund appropriated from profit after taxation in the financial statements prepared under PRC Accounting Standards and Systems. Under HKFRS, it was recognised as expenses in the income statement of the year.
14. The Group's investment properties were revalued this year. The change in the fair value was recognised in the income statement under HKFRS.
15. The gain from the disposal of fixed assets by a subsidiary of the Company was recognised as capital reserve in financial statements prepared in accordance with PRC Accounting Standards and Systems. Under HKFRS, it was recognised in the income statement.



# NOTES TO THE FINANCIAL STATEMENTS

## XVIII. OPINION OF REVIEW ON THE STATEMENT OF ADJUSTMENT ON THE DIFFERENCES OF CONSOLIDATED SHAREHOLDERS' EQUITY ARISING FROM ADOPTION OF THE PREVIOUS AND THE NEW ACCOUNTING STANDARDS

To All Shareholders of Guangzhou Pharmaceutical Company Limited,

We have reviewed the attached statement of adjustment on the differences of Consolidated shareholders' equity arising from adoption of the previous and the new accounting standards (hereinafter referred to as "the statement of difference adjustment") of Guangzhou Pharmaceutical Company Limited (hereinafter referred to as "the Company") as well as the notes to its preparation. It is the responsibilities of the management of the Company to prepare the statement of difference adjustment in accordance with the relevant regulations of Accounting Standards for Business Enterprises No. 38 °V Adoption of Accounting Standards for Business Enterprises for the First Time and the "Notice on Fulfillment of Financial and Accounting Information Disclosures Related to the New Accounting Standards" (with reference of ZJF [2006] No. 136, hereinafter referred to as "the Notice"). Our responsibility is to render a report on the statement of difference adjustment based on our review.

Pursuant to the relevant stipulations of the Notice, we conduct our review in accordance with the regulations of Standard on Review Engagements for CPAs of China No. 2101 — Review on Financial Statements. The said standard requires that we plan and perform the review to obtain limited assurance whether the statement of difference adjustment is free from material misstatement. The review mainly limits to enquiry of the related personnel of the Company regarding the relevant accounting policies and all the significant assertions of the statement of different adjustment; comprehension of computation process of the adjusted amounts in the statement of difference adjustment and; review of the statement of difference adjustment in order to consider whether or not the statement of difference adjustment is prepared on the designated basis and analytical procedure is performed when necessary. The degree of assurance provided by review is lower than that by audit. As we have not performed audit, no audit opinion is expressed accordingly.

Based on our review, we have not noticed any affairs that makes us believe the statement of difference adjustment is not prepared in accordance with the relevant regulations of Accounting Standards for Business Enterprises No. 38 - Adoption of Accounting Standards for Business Enterprises for the First Time and the Notice.

In addition, we remind the users of the statement of difference adjustment that as mentioned in Point IV of the accompanying notes to preparation of the statement of difference adjustment, the amount of consolidated shareholders' equity as of January 1, 2007 (by adoption of the new accounting standards) in the statement of difference adjustment of the Company may be different from the relevant amounts in the financial statements for the year 2007. For better understanding of the statement of difference adjustment, the accompanying statement of difference adjustment should be read along with the audited financial statements of the Company.

Appended statement: The Statement of Adjustment on the Differences of Consolidated Shareholders' Equity Arising from Adoption of the Previous and the New Accounting Standards

Guangdong Yangcheng Certified Public Accountants Co., Ltd.

Chinese Certified Public Accountant  
**Wu Jiali**

Guangzhou, China  
April 27, 2007

Chinese Certified Public Accountant  
**Ye Weixiang**



# NOTES TO THE FINANCIAL STATEMENTS

## XVIII. OPINION OF REVIEW ON THE STATEMENT OF ADJUSTMENT ON THE DIFFERENCES OF CONSOLIDATED SHAREHOLDERS' EQUITY ARISING FROM ADOPTION OF THE PREVIOUS AND THE NEW ACCOUNTING STANDARDS

(Continued)

### Statement of Adjustment on the Differences of Consolidated Shareholders' Equity Arising from Adoption of the Previous and the New Accounting Standards

Prepared by: Guangzhou Pharmaceutical Company Limited

Monetary unit: RMB Yuan

No.	Items	Amount
	<b>Shareholders' equity as of December 31, 2006 (the prevailing accounting standards)</b>	<b>2,788,087,947.63</b>
1	Difference in long-term equity investment Including: Difference in long-term equity arising from merger of enterprises under the same control	(2,284,742.40) (2,284,742.40)
	Credited difference in other long-term equity investment accounted for by equity method	—
2	Investment housing property to be accounted for under fair value model	—
3	Additional depreciation etc. to be accrued for the previous years due to the estimated expenses of discarding and disposal of assets	—
4	Demission compensation eligible for recognizing as estimated liabilities	—
5	Share-based payment	—
6	Restructuring obligations eligible for recognizing as estimated liabilities	—
7	Merger of enterprises Including: book value of goodwill in the merger of enterprises under the same control	(911,601.45) —
	Provision for impairment of goodwill accrued by adopting the new accounting standards	(911,601.45)
8	Financial assets and available-for-sales financial assets at fair values through profit or loss	—
9	Financial liabilities at fair values through profit or loss	—
10	Equity increased for the separation of the financial instruments	—
11	Derivative financial instruments	—
12	Income tax	60,643,787.47
13	Minority shareholders' equity	166,444,059.04
14	Others	—
(1)	Transitional medical insurance for retired staff eligibly recognized as estimated liabilities	(55,071,212.41)
(2)	Changes in consolidation scope by adopting the new accounting standards	(99,592.74)
	<b>Shareholders' equity as of January 1, 2007 (the new accounting standards)</b>	<b><u>2,956,808,645.14</u></b>



# INDEPENDENT AUDITOR'S REPORT

## To the shareholders of Guangzhou Pharmaceutical Company Limited

*(a joint stock company established in the People's Republic of China with limited liability)*

We have audited the consolidated financial statements of Guangzhou Pharmaceutical Company Limited (the "Company") and its subsidiaries (together, the "Group") set out on pages 138 to 191, which comprise the consolidated and Company balance sheets as at 31 December 2006, and the consolidated income statement, the consolidated statement of changes in equity and the consolidated cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory Notes.

## DIRECTORS' RESPONSIBILITY FOR THE FINANCIAL STATEMENTS

The directors of the Company are responsible for the preparation and the true and fair presentation of these consolidated financial statements in accordance with Hong Kong Financial Reporting Standards issued by the Hong Kong Institute of Certified Public Accountants and the disclosure requirements of the Hong Kong Companies Ordinance. This responsibility includes designing, implementing and maintaining internal control relevant to the preparation and the true and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

## AUDITOR'S RESPONSIBILITY

Our responsibility is to express an opinion on these consolidated financial statements based on our audit and to report our opinion solely to you, as a body, and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report.

We conducted our audit in accordance with Hong Kong Standards on Auditing issued by the Hong Kong Institute of Certified Public Accountants. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance as to whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and true and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the directors, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

## OPINION

In our opinion, the consolidated financial statements give a true and fair view of the state of affairs of the Company and of the Group as at 31 December 2006 and of the Group's profit and cash flows for the year then ended in accordance with Hong Kong Financial Reporting Standards and have been properly prepared in accordance with the disclosure requirements of the Hong Kong Companies Ordinance.

### **PricewaterhouseCoopers**

Certified Public Accountants

Hong Kong, 27 April 2007



# CONSOLIDATED BALANCE SHEET

As at 31 December 2006

		As at 31 December	
	Note	2006 RMB'000	2005 RMB'000
<b>ASSETS</b>			
<b>Non-current assets</b>			
Property, plant and equipment	6	1,478,262	1,542,068
Investment properties	7	35,413	8,712
Land use rights	8	127,800	134,691
Intangible assets	9	40,629	49,506
Investments in associates	11	44,085	4,854
Available-for-sale financial assets	13	30,225	61,994
Deferred income tax assets	21	64,952	53,345
		<u>1,821,366</u>	<u>1,855,170</u>
<b>Current assets</b>			
Inventories	14	1,326,444	1,148,569
Trade and other receivables	15	2,004,026	1,683,197
Financial assets at fair value through profit or loss		—	10,903
Bank and cash balances	16	489,128	618,581
		<u>3,819,598</u>	<u>3,461,250</u>
<b>Total assets</b>		<u><b>5,640,964</b></u>	<u><b>5,316,420</b></u>
<b>EQUITY</b>			
<b>Capital and reserves attributable to equity holders of the Company</b>			
Share capital	17	1,592,034	1,592,034
Other reserves	18	1,085,486	989,014
Retained earnings			
— Proposed final dividend	30	68,116	56,763
— Others		151,753	85,312
		<u>2,897,389</u>	<u>2,723,123</u>
<b>Minority interest</b>		<u>182,991</u>	<u>201,707</u>
<b>Total equity</b>		<u><b>3,080,380</b></u>	<u><b>2,924,830</b></u>
<b>LIABILITIES</b>			
<b>Non-current liabilities</b>			
Deferred income tax liabilities	21	41,870	42,522
Employee benefits	22	50,138	46,203
		<u>92,008</u>	<u>88,725</u>
<b>Current liabilities</b>			
Trade and other payables	19	1,537,900	1,359,720
Current income tax liabilities		42,477	25,360
Borrowings	20	888,199	917,785
		<u>2,468,576</u>	<u>2,302,865</u>
<b>Total liabilities</b>		<u><b>2,560,584</b></u>	<u><b>2,391,590</b></u>
<b>Total equity and liabilities</b>		<u><b>5,640,964</b></u>	<u><b>5,316,420</b></u>
<b>Net current assets</b>		<u><b>1,351,022</b></u>	<u><b>1,158,385</b></u>
<b>Total assets less current liabilities</b>		<u><b>3,172,388</b></u>	<u><b>3,013,555</b></u>

Shi Shaobin  
Director

Feng Zansheng  
Director

The Notes on pages 143 to 191 are an integral part of these consolidated financial statements.

# BALANCE SHEET

As at 31 December 2006

		As at 31 December	
	Note	2006 RMB'000	2005 RMB'000
<b>ASSETS</b>			
<b>Non-current assets</b>			
Property, plant and equipment	6	21,832	24,613
Intangible assets	9	729	972
Investments in subsidiaries	10	1,460,126	1,413,712
Investments in associates	11	2,120	2,179
Investments in jointly controlled entities	12	102,035	102,035
Available-for-sale financial assets	13	27,288	58,683
Deferred income tax assets	21	4,687	—
		<b>1,618,817</b>	<b>1,602,194</b>
<b>Current assets</b>			
Inventories	14	9,974	—
Trade and other receivables	15	798,678	638,420
Financial assets at fair value through profit or loss		—	10,903
Bank and cash balances	16	64,731	90,103
		<b>873,383</b>	<b>739,426</b>
<b>Total assets</b>		<b>2,492,200</b>	<b>2,341,620</b>
<b>EQUITY</b>			
<b>Capital and reserves attributable to equity holders of the Company</b>			
Share capital	17	1,592,034	1,592,034
Other reserves	18	604,450	580,113
Retained earnings			
— Proposed final dividend		68,116	56,763
— Others		148,750	57,943
<b>Total equity</b>		<b>2,413,350</b>	<b>2,286,853</b>
<b>LIABILITIES</b>			
<b>Current liabilities</b>			
Trade and other payables	19	42,099	54,767
Current income tax liabilities		6,751	—
Borrowings	20	30,000	—
		<b>78,850</b>	<b>54,767</b>
<b>Total equity and liabilities</b>		<b>2,492,200</b>	<b>2,341,620</b>

Shi Shaobin  
Director

Feng Zansheng  
Director

The Notes on pages 143 to 191 are an integral part of these consolidated financial statements.





# CONSOLIDATED INCOME STATEMENT

For the year ended 31 December 2006

		Year ended 31 December	
	Note	2006 RMB'000	2005 RMB'000
<b>Sales</b>	5	<b>10,241,004</b>	9,026,340
Cost of goods sold	24	<b>(8,472,228)</b>	(7,472,974)
<b>Gross profit</b>		<b>1,768,776</b>	1,553,366
Other income - net	23	<b>75,196</b>	91,594
Selling and marketing costs	24	<b>(778,181)</b>	(616,821)
Administrative expenses	24	<b>(656,513)</b>	(641,365)
Other operating losses - net		<b>(14,484)</b>	(16,459)
<b>Operating profit</b>		<b>394,794</b>	370,315
Finance costs - net	26	<b>(45,360)</b>	(53,610)
Share of losses of associates	11	<b>(279)</b>	(1,212)
<b>Profit before income tax</b>		<b>349,155</b>	315,493
Income tax expense	27	<b>(118,567)</b>	(107,771)
<b>Profit for the year</b>		<b>230,588</b>	207,722
<b>Attributable to:</b>			
Equity holders of the Company	28	<b>218,067</b>	197,804
Minority interest		<b>12,521</b>	9,918
		<b>230,588</b>	207,722
<b>Earnings per share for profit attributable to equity holders of the Company during the year (expressed in RMB per share)</b>			
— basic and diluted	29	<b>0.269</b>	0.244
<b>Dividend</b>	30	<b>68,116</b>	56,763



The Notes on pages 143 to 191 are an integral part of these consolidated financial statements.

# CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

For the year ended 31 December 2006

	Attributable to equity holders of the Company				Minority interest	Total equity
	Note	Share capital	Other reserves	Retained earnings		
		RMB'000	RMB'000	RMB'000	RMB'000	RMB'000
<b>Balance at 1 January 2005</b>		1,592,034	880,427	73,131	2,545,592	2,757,879
Profit for the year		—	—	197,804	197,804	207,722
Dividend relating to 2004		—	—	(20,273)	(20,273)	(30,056)
Transfers		—	98,684	(98,684)	—	—
Impact arising from dilution of equity interest in a subsidiary (the subsidiary became a jointly controlled entity subsequent to the dilution)		—	9,903	(9,903)	—	(10,715)
<b>Balance at 31 December 2005</b>		<u>1,592,034</u>	<u>989,014</u>	<u>142,075</u>	<u>2,723,123</u>	<u>2,924,830</u>
<b>Balance at 1 January 2006</b>		1,592,034	989,014	142,075	2,723,123	2,924,830
Profit for the year		—	—	218,067	218,067	230,588
Dividend relating to 2005	30	—	—	(56,763)	(56,763)	(68,977)
Revaluation of investment properties	7	—	13,116	—	13,116	14,634
Acquisition of interests in subsidiaries from minority shareholders		—	—	—	—	(19,723)
Disposal of a subsidiary		—	(154)	—	(154)	(972)
Transfers		—	83,510	(83,510)	—	—
<b>Balance at 31 December 2006</b>		<u>1,592,034</u>	<u>1,085,486</u>	<u>219,869</u>	<u>2,897,389</u>	<u>3,080,380</u>



The Notes on pages 143 to 191 are an integral part of these consolidated financial statements.

# CONSOLIDATED CASH FLOW STATEMENT

For the year ended 31 December 2006

		Year ended 31 December	
	Note	2006 RMB'000	2005 RMB'000
<b>Cash flows from operating activities</b>			
Cash generated from operations	31	140,561	238,886
Interest paid		(46,275)	(51,211)
Income tax paid		(113,709)	(121,933)
		<u>          </u>	<u>          </u>
Net cash (used in)/generated from operating activities		(19,423)	65,742
<b>Cash flows from investing activities</b>			
Payment for acquisition of interests in subsidiaries from minority shareholders		(18,298)	—
Cash contribution paid to associates		(25,221)	—
Disposal of a subsidiary, net of cash held	31	(802)	—
Purchase of property, plant and equipment		(27,302)	(31,693)
Purchase of construction in progress		(59,507)	(93,597)
Proceeds from sale of property, plant and equipment	31	5,710	1,230
Purchase of intangible assets		(1,515)	(500)
Purchase of land use rights		(2,788)	—
Government grants received		9,917	28,721
Disposal/(purchase) of available-for-sale financial assets		30,000	(200)
Disposal of financial assets at fair value through profit or loss		14,690	—
Cash received from disposal of interests in associates		1,400	—
Interest received		9,753	10,522
Dividend received from a jointly controlled entity, net of impact arising from proportionate consolidation		4,177	—
Dividend received from available-for-sale financial assets		4,567	3,405
		<u>          </u>	<u>          </u>
Net cash used in investing activities		(55,219)	(82,112)
<b>Cash flows from financing activities</b>			
Capital contribution from minority shareholders		—	62,627
Proceeds from borrowings		1,137,401	1,341,918
Repayments of borrowings		(1,124,719)	(1,621,923)
Dividend paid to equity holders of the Company		(55,279)	(20,273)
Dividend paid to minority interest		(12,214)	(9,783)
		<u>          </u>	<u>          </u>
Net cash used in financing activities		(54,811)	(247,434)
<b>Net decrease in bank and cash balances</b>		<b>(129,453)</b>	<b>(263,804)</b>
Bank and cash balances at beginning of the year		<u>618,581</u>	<u>882,385</u>
<b>Bank and cash balances at end of the year</b>	16	<u><b>489,128</b></u>	<u>618,581</u>

The Notes on pages 143 to 191 are an integral part of these consolidated financial statements.



# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(prepared in accordance with HKFRS)

## 1. GENERAL INFORMATION

Guangzhou Pharmaceutical Company Limited (the "Company") was established as a joint stock company with limited liability in the People's Republic of China (the "PRC") on 1 September 1997. Its H shares have been listed on The Stock Exchange of Hong Kong Limited since 30 October 1997 and its A shares have been listed on The Shanghai Stock Exchange since 6 February 2001. The Company and its subsidiaries (together, the "Group") are principally engaged in the manufacture of Chinese Patent Medicine ("CPM"), the wholesale, retail, import and export of western pharmaceutical products, CPM and medical apparatus and the wholesale, retail of Chinese raw medicine.

The address of its registered office is 45 Sha Mian North Street, Guangzhou City, Guangdong Province, PRC.

These consolidated financial statements are presented in thousands of units of RMB (RMB'000), unless otherwise stated. These consolidated financial statements have been approved for issue by the Board of Directors on 27 April 2007.

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The principal accounting policies applied in the preparation of these consolidated financial statements are set out below. These policies have been consistently applied to all the years presented, unless otherwise stated.

### 2.1 Basis of preparation

The consolidated financial statements of the Company have been prepared in accordance with Hong Kong Financial Reporting Standards ("HKFRS"). The consolidated financial statements have been prepared under the historical cost convention, as modified by the revaluation of investment properties, available-for-sale financial assets, financial assets and financial liabilities at fair value through profit or loss, which are carried at fair value.

The preparation of financial statements in conformity with HKFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Group's accounting policies. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements, are disclosed in Note 4.

- (a) Standards, interpretations and amendments to published standards effective in 2006 but not relevant to the Group's operations.

The following standards, amendments and interpretations are mandatory for accounting periods beginning on or after 1 January 2006. They are not relevant to the Group's operations.

HKAS 1 (Amendment)	First-time Adoption of Hong Kong Financial Reporting Standards
HKAS 19 (Amendment)	Actuarial Gains and Losses, Group Plans and Disclosures
HKAS 21 (Amendment)	Net Investment in a Foreign Operation
HKAS 39 (Amendment)	Cash Flow Hedge Accounting of Forecast Intragroup Transactions
HKAS 39 (Amendment)	The Fair Value Option
HKFRS 6	Exploration for and Evaluation of Mineral Resources
HKFRS-int 3	Emission Rights
HKFRS-int 4	Determining whether an Arrangement Contains a Lease
HKFRS-int 5	Rights to Interests arising from Decommissioning, Restoration and Environmental Rehabilitation Funds
HK(IFRIC)-Int 6	Liabilities arising from Participating in a Specific Market - Waste Electrical and Electronic Equipment



# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(prepared in accordance with HKFRS)

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### 2.1 Basis of preparation (Continued)

- (b) Amendments to published standards effective in 2006 and are relevant to the Group's operations.

The following amendments are mandatory for accounting periods beginning on or after 1 January 2006. They are relevant to the Group's operations but the impact is not significant.

HKAS 39 and HKFRS 4 (Amendment) Financial Guarantee Contracts

- (c) Standards, interpretations and amendments to published standards that are not yet effective and have not been early adopted by the Group

HKFRS 7	Financial Instruments: Disclosure <sup>1</sup>
HK(IFRIC)-Int 7	Applying the Restatement Approach under HKFRS 29 <sup>2</sup>
HK(IFRIC)-Int 8	Scope of HKFRS 2 <sup>3</sup>
HK(IFRIC)-Int 9	Reassessment of Embedded Derivatives <sup>4</sup>
HK(IFRIC)-Int 10	Interim Financial Reporting and Impairment <sup>5</sup>

<sup>1</sup> Effective for accounting periods commencing on or after 1 January 2007

<sup>2</sup> Effective for accounting periods commencing on or after 1 March 2006

<sup>3</sup> Effective for accounting periods commencing on or after 1 May 2006

<sup>4</sup> Effective for accounting periods commencing on or after 1 June 2006

<sup>5</sup> Effective for accounting periods commencing on or after 1 November 2006

### 2.2 Consolidation

The consolidated financial statements include the financial statements of the Company and all of its subsidiaries made up to 31 December.

- (a) Subsidiaries

Subsidiaries are all entities over which the Group has the power to govern the financial and operating policies generally accompanying a shareholding of more than one half of the voting rights. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether the Group controls another entity.

Subsidiaries are fully consolidated from the date on which control is transferred to the Group. They are de-consolidated from the date that control ceases.

The purchase method of accounting is used to account for the acquisition of subsidiaries by the Group. The cost of an acquisition is measured as the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange, plus costs directly attributable to the acquisition. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date, irrespective of the extent of any minority interest. The excess of the cost of acquisition over the fair value of the Group's share of the identifiable net assets acquired is recorded as goodwill. If the cost of acquisition is less than the fair value of the net assets of the subsidiary acquired, the difference is recognised directly in the income statement (Note 2.8).



# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(prepared in accordance with HKFRS)

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### 2.2 Consolidation (Continued)

#### (a) Subsidiaries (Continued)

Inter-company transactions, balances and unrealised gains on transactions between group companies are eliminated. Unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. Accounting policies of subsidiaries have been changed where necessary to ensure consistency with the policies adopted by the Group.

In the Company's balance sheet the investments in subsidiaries are stated at cost less provision for impairment losses. The results of subsidiaries are accounted by the Company on the basis of dividend received and receivable.

#### (b) Associates

Associates are all entities over which the Group has significant influence but not control, generally accompanying a shareholding of between 20% and 50% of the voting rights. Investments in associates are accounted for using the equity method of accounting and are initially recognised at cost. The Group's investment in associates includes goodwill (net of any accumulated impairment loss) identified on acquisition (Note 2.8).

The Group's share of its associates' post-acquisition profits or losses is recognised in the income statement, and its share of post-acquisition movements in reserves is recognised in reserves. The cumulative post-acquisition movements are adjusted against the carrying amount of the investment. When the Group's share of losses in an associate equals or exceeds its interest in the associate, including any other unsecured receivables, the Group does not recognise further losses, unless it has incurred obligations or made payments on behalf of the associate.

Unrealised gains on transactions between the Group and its associates are eliminated to the extent of the Group's interest in the associates. Unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. Accounting policies of associates have been changed where necessary to ensure consistency with the policies adopted by the Group.

Dilution gains and losses in associates are recognised in the consolidated income statement.

In the Company's balance sheet the investments in associated companies are stated at cost less provision for impairment losses. The results of associated companies are accounted for by the Company on the basis of dividend received and receivable.



# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(prepared in accordance with HKFRS)

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### 2.2 Consolidation (Continued)

#### (c) Joint ventures

The Group's interests in jointly controlled entities are accounted for by proportionate consolidation. The Group combines its share of the jointly controlled entities' individual income and expenses, assets and liabilities and cash flows on a line-by-line basis with similar items in the Group's financial statements. The Group recognises the portion of gains or losses on the sale of assets by the Group to the jointly controlled entities that it is attributable to the other venturers. The Group does not recognise its share of profits or losses from the jointly controlled entities that result from the Group's purchase of assets from the jointly controlled entities until it resells the assets to an independent party. However, a loss on the transaction is recognised immediately if the loss provides evidence of a reduction in the net realisable value of current assets, or an impairment loss.

In the Company's balance sheet, the investments in jointly controlled entities are stated at cost less provision for impairment losses. The results of jointly controlled entities are accounted for by the Company on the basis of dividend received and receivable.

### 2.3 Segment reporting

A business segment is a group of assets and operations engaged in providing products or services that are subject to risks and returns that are different from those of other business segments. A geographical segment is engaged in providing products or services within a particular economic environment that is subject to risks and returns that are different from those of segments operating in other economic environments.

### 2.4 Foreign currency translation

#### (a) Functional and presentation currency

Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates (the "functional currency"). The consolidated financial statements are presented in Renminbi, which is the Company's functional and presentation currency.

#### (b) Transactions and balances

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the income statement.



# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(prepared in accordance with HKFRS)

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### 2.5 Property, plant and equipment

Property, plant and equipment are stated at historical cost less accumulated depreciation and impairment losses. Historical cost includes expenditure that is directly attributable to the acquisition of the items.

Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. The carrying amount of the replaced part is derecognised. All other repairs and maintenance are charged in the income statement during the financial period in which they are incurred.

Depreciation of property, plant and equipment is calculated using the straight-line method to allocate their costs to their residual values over their estimated useful lives, as follows:

Plant and buildings	15 - 50 years
Machinery and equipment	4 - 18 years
Motor vehicles	5 - 10 years

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each balance sheet date.

An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount (Note 2.10).

Gains and losses on disposals are determined by comparing the proceeds with the carrying amount and are recognised within other operating losses — net, in the income statement. When revalued assets are sold, the amounts included in other reserves are transferred to retained earnings.

### 2.6 Investment properties

Property that is held for long-term rental yields or for capital appreciation or both, and that is not occupied by the companies in the consolidated Group, is classified as investment property.

Investment property comprises land held under operating leases. Land held under operating leases are classified and accounted for as investment property when the rest of the definition of investment property is met. The operating lease is accounted for as if it were a finance lease.

Investment property is measured initially at its cost, including related transaction costs.

After initial recognition, investment property is carried at fair value. Fair value is based on active market prices, adjusted, if necessary, for any difference in the nature, location or condition of the specific asset. If this information is not available, the Group uses alternative valuation methods such as recent prices on less active markets or discounted cash flow projections. These valuations are reviewed annually by external valuers. Investment property that is being redeveloped for continuing use as investment property or for which the market has become less active continues to be measured at fair value.

The fair value of investment property reflects, among other things, rental income from current leases and assumptions about rental income from future leases in the light of the usage of individual properties and current market conditions.





# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(prepared in accordance with HKFRS)

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### 2.6 Investment properties (Continued)

Subsequent expenditure is charged to the asset's carrying amount only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. All other repairs and maintenance costs are expensed in the income statement during the financial period in which they are incurred.

Changes in fair values are recognised in the income statement as part of other income - net.

If an investment property becomes owner-occupied, it is reclassified as property, plant and equipment, and its fair value at the date of reclassification becomes its cost for accounting purposes. Property that is being constructed or developed for future use as investment property is classified as property, plant and equipment and stated at cost until construction or development is complete, at which time it is reclassified and subsequently accounted for as investment property.

If an item of property, plant and equipment becomes an investment property because its use has changed, any difference resulting between the carrying amount and the fair value of this item at the date of transfer is recognised in equity as a revaluation of property, plant and equipment under HKAS 16. However, if a fair value gain reverses a previous impairment loss, the gain is recognised in the income statement.

Investment property held for sale without redevelopment is classified within non-current assets held for sale, under HKFRS 5.

### 2.7 Land use rights

Land use rights are stated at cost less accumulated amortisation and accumulated impairment losses.

Amortisation of land use rights is calculated to write off their cost less accumulated impairment losses on a straight-line basis over the remaining unexpired land use period of 20 to 50 years.

### 2.8 Intangible assets

#### (a) Goodwill

Goodwill represents the excess of the cost of an acquisition over the fair value of the Group's share of the net identifiable assets of the acquired subsidiary/associate/jointly controlled entity at the date of acquisition. Goodwill on acquisitions of subsidiaries and jointly controlled entities is included in intangible assets. Goodwill on acquisitions of associates is included in investments in associates and is tested annually for impairment as part of the overall balance. Separately recognised goodwill is tested annually for impairment and carried at cost less accumulated impairment losses. Impairment losses on goodwill are not reversed. Gains and losses on the disposal of an entity include the carrying amount of goodwill relating to the entity sold.

Goodwill is allocated to cash-generating units for the purpose of impairment testing. The allocation is made to those cash-generating units or groups of cash-generating units that are expected to benefit from the business combination in which the goodwill arose.



# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(prepared in accordance with HKFRS)

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### 2.8 Intangible assets (Continued)

(b) Patents and trademarks

Patents and trademarks are shown at historical cost. Patents and trademarks have a finite useful life and are carried at cost less accumulated amortisation. Amortisation is calculated using the straight-line method to allocate the cost of patents and trademarks over their estimated useful lives (less than 20 years).

(c) Staff quarters reform costs

Staff quarters reform costs are expenditures incurred by the Group prior to year 2000 in relation to purchases of staff quarters by its employees. Such costs are recognised as an asset. These costs are amortised on a straight-line basis over a period of not more than 10 years to reflect the estimated remaining average service life of the employees of the Group in which the related economic benefits are recognised.

(d) Computer software

Acquired computer software licences are capitalised on the basis of the costs incurred to acquire and bring to use the specific software. These costs are amortised on a straight-line basis over their estimated useful lives (three to five years).

### 2.9 Research and development

Research expenditure is recognised as an expense as incurred. Costs incurred on development projects (relating to the design and testing of new or improved products) are recognised as intangible assets when the following criteria are fulfilled:

- (a) it is technically feasible to complete the intangible asset so that it will be available for use or sale;
- (b) management intends to complete the intangible asset and use or sell it;
- (c) there is an ability to use or sell the intangible asset;
- (d) it can be demonstrated how the intangible asset will generate probable future economic benefits;
- (e) adequate technical, financial and other resources to complete the development and to use or sell the intangible asset are available; and
- (f) the expenditure attributable to the intangible asset during its development can be reliably measured.

Other development expenditures that do not meet these criteria are recognised as an expense as incurred. Development costs previously recognised as an expense are not recognised as an asset in a subsequent period. Capitalised development costs are recorded as intangible assets and amortised from the point at which the asset is ready for use on a straight-line basis over its useful life.

Development assets are tested for impairment annually, in accordance with HKAS 36.



# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(prepared in accordance with HKFRS)

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### 2.10 Impairment of investments in subsidiaries, jointly controlled entities, associates and non-financial assets

Assets that have an indefinite useful life or have not yet available for use are not subject to amortisation and are tested annually for impairment or are tested for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. Assets that are subject to amortisation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units). Assets other than goodwill that suffered an impairment are reviewed for possible reversal of the impairment at each reporting date.

### 2.11 Financial assets

The Group classifies its financial assets in the following categories: at fair value through profit or loss, loans and receivable and available-for-sale. The classification depends on the purposes for which the financial assets were acquired. Management determine the classification of its financial assets at initial recognition.

- (a) Financial assets at fair value through profit or loss

Financial assets at fair value through profit or loss are financial assets held for trading. A financial asset is classified in this category if acquired principally for the purpose of selling in the short term. Assets in this category are classified as current assets.

- (b) Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They are included in current assets, except for maturities greater than 12 months after the balance sheet date. These are classified as non-current assets. Loans and receivables are classified as trade and other receivables in the balance sheet (Note 2.13).

- (c) Available-for-sale financial assets

Available-for-sale financial assets are non-derivatives that are either designated in this category or not classified in any of the other categories. They are included in non-current assets unless management intends to dispose of the investment within 12 months of the balance sheet date.

Regular purchases and sales of financial assets are recognised on the trade-date - the date on which the Group commits to purchase or sell the asset. Investments are initially recognised at fair value plus transaction costs for all financial assets not carried at fair value through profit or loss. Financial assets carried at fair value through profit or loss are initially recognised at fair value, and transaction costs are expensed in the income statement. Financial assets are derecognised when the rights to receive cash flows from the investments have expired or have been transferred and the Group has transferred substantially all risks and rewards of ownership. Available-for-sale financial assets and financial assets at fair value through profit or loss are subsequently carried at fair value. Loans and receivables are carried at amortised cost using the effective interest method.



# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(prepared in accordance with HKFRS)

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### 2.11 Financial assets (Continued)

#### (c) Available-for-sale financial assets (Continued)

Gains or losses arising from changes in the fair value of the 'financial assets at fair value through profit or loss' category are presented in the income statement within "other income - net", in the period in which they arise. Dividend income from financial assets at fair value through profit or loss is recognised in the income statement as part of "other income - net" when the Group's right to receive payments is established.

When securities classified as available for sale are sold or impaired, the accumulated fair value adjustments recognised in equity are included in the income statement as gains and losses from investment securities.

Interest on available-for-sale securities calculated using the effective interest method is recognised in the income statement as part of "other income - net". Dividends on available-for-sale equity instruments are recognised in the income statement as part of "other income - net" when the Group's right to receive payments is established.

The fair values of quoted investments are based on current bid prices. If the market for a financial asset is not active (and for unlisted securities), the Group established fair value by using valuation techniques. These include the use of recent arm's length transactions, reference to other instruments that are substantially the same, discounted cash flow analysis and option pricing models, making maximum use of market inputs and relying as little as possible on entity-specific inputs.

The Group assesses at each balance sheet date whether there is objective evidence that a financial asset or a group of financial assets is impaired. In the case of equity securities classified as available for sale, a significant or prolonged decline in the fair value of the security below its cost is considered as an indicator that the securities are impaired. If any such evidence exists for available-for-sale financial assets, the cumulative loss - measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that financial asset previously recognised in profit or loss - is removed from equity and recognised in the income statement. Impairment losses recognised in the income statement on equity instruments are not reversed through the income statement. Impairment testing of trade receivables is described in Note 2.13.

### 2.12 Inventories

Inventories are stated at the lower of cost and net realisable value. Cost is determined using the weighted average method. The cost of finished goods and work in progress comprises raw materials, direct labour, other direct costs and related production overheads (based on normal operating capacity). It excludes borrowing costs. Net realisable value is the estimated selling price in the ordinary course of business, less applicable variable selling expenses.



# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(prepared in accordance with HKFRS)

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### 2.13 Trade and other receivables

Trade and other receivables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method, less provision for impairment. A provision for impairment of trade and other receivables is established when there is objective evidence that the Group will not be able to collect all amounts due according to the original terms of the receivables. Significant financial difficulties of the debtor, probability that the debtor will enter bankruptcy or financial reorganisation, and default or delinquency in payments are considered indicators that the trade receivable is impaired. The amount of the provision is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the original effective interest rate. The carrying amount of the assets is reduced through the use of an allowance account, and the amount of the loss is recognised in the income statement within "administrative expenses". When a trade receivable is uncollectible, it is written off against the allowance account for trade receivables. Subsequent recoveries of amounts previously written off are credited against "administrative expenses" in the income statement.

### 2.14 Cash and cash equivalent

Cash and cash equivalent refers to cash in hand and deposits held at call with banks.

### 2.15 Share capital

Ordinary shares are classified as equity.

Incremental costs directly attributable to the issue of new shares are shown in equity as a deduction, net of tax, from the proceeds.

### 2.16 Trade payables

Trade payables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method.

### 2.17 Borrowings

Borrowings are recognised initially at fair value, net of transaction costs incurred. Borrowings are subsequently stated at amortised cost; any difference between the proceeds (net of transaction costs) and the redemption value is recognised in the income statement over the period of the borrowings using the effective interest method.

Borrowings are classified as current liabilities unless the Group has an unconditional right to defer settlement of the liability for at least 12 months after the balance sheet date.

Borrowing costs incurred for the construction of any qualifying asset are capitalised during the period of time that is required to complete and prepare the asset for its intended use. Other borrowing costs are expensed.



# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(prepared in accordance with HKFRS)

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### 2.18 Deferred income tax

Deferred income tax is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. However, the deferred income tax is not accounted for if it arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit or loss. Deferred income tax is determined using tax rates (and laws) that have been enacted or substantially enacted by the balance sheet date and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled.

Deferred income tax assets are recognised to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised.

Deferred income tax is provided on temporary differences arising on investments in subsidiaries, associates and jointly controlled entities, except where the timing of the reversal of the temporary difference is controlled by the Group and it is probable that the temporary difference will not reverse in the foreseeable future.

### 2.19 Employee benefits

#### (a) Pension obligations

The Group participates in the defined contribution employee retirement schemes regarding pension benefits required under existing PRC legislation. The defined contribution plan is a pension plan under which the Group pays contributions into a separate entity. The Group has no legal or constructive obligations to pay further contributions if the fund does not hold sufficient assets to pay all employees the benefits relating to employee service in the current and prior periods. The Group's obligations include contributions to a defined contribution retirement plan at a certain percentage of the salaries of the employees. The regular contributions are charged to the income statement when services are rendered by the employees. Once the contributions have been paid, the Group has no further payment obligations.

#### (b) Housing benefit

The Group's contributions to the defined contribution housing fund scheme administered by a government agency determined at a certain percentage of the salaries of the employees are expensed when services are rendered by the employees.

Costs of the housing allowance scheme designed and implemented by the Group are expensed when a legal or constructive obligation is established.

#### (c) Medical insurance

The Group's contributions to the defined contribution medical insurance scheme administered by a government agency for existing employees are expensed when services are rendered by the employees.

Contributions to the defined contribution medical insurance scheme for retired and retiring employees are accrued based on the period of their past services. Where the contributions do not fall due wholly within twelve months, the contributions payable are discounted using the discount rate determined by reference to market yields at the balance sheet date on high quality investments.

#### (d) Profit-sharing and bonus plans

The Group recognises a liability and an expense for bonuses and profit-sharing, based on a formula that takes into consideration the profit attributable to equity holders of the Company after certain adjustments. The Group recognises a provision where contractually obliged or where there is a past practice that has created a constructive obligation.



# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(prepared in accordance with HKFRS)

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### 2.20 Revenue recognition

Revenue comprises the fair value of the consideration received or receivable for the sale of goods and services in the ordinary course of the Group's activities. Revenue is shown net of value-added tax, returns, rebates and discounts and after eliminating sales within the Group.

The Group recognises revenue when the amount of revenue can be reliably measured, it is probable that future economic benefits will flow to the entity and specific criteria have been met for each of the Group's activities as described below. The amount of revenue is not considered to be reliably measurable until all contingencies relating to the sale have been resolved. The Group bases its estimates on historical results, taking into consideration the type of customer, the type of transaction and the specifics of each arrangement.

(a) Sales of goods — wholesale

Sales of goods are recognised when an entity in the Group has delivered products to the customer, the customer has accepted the products and collectibility of the related receivables is reasonably assured.

(b) Sales of goods — retail

Sales of goods are recognised when an entity in the Group sells a product to the customer. Retail sales are usually in cash or by credit card. The recorded revenue includes credit card fees payable for the transaction. Such fees are included in "selling and marketing costs".

(c) Interest income

Interest income is recognised on a time-proportion basis using the effective interest method. When a receivable is impaired, the Group reduces the carrying amount to its recoverable amount, being the estimated future cash flow discounted at original effective interest rate of the instrument, and continues unwinding the discount as interest income. Interest income on impaired loans is recognised using the original effective interest rate.

(d) Royalty income

Royalty income is recognised on an accruals basis in accordance with the substance of the relevant agreements.

(e) Dividend income

Dividend income is recognised when the right to receive payment is established.

### 2.21 Leases (as the lessee for operating leases)

Leases in which a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. Payments made under operating leases (net of any incentives received from the lessor) are charged to the income statement on a straight-line basis over the period of the lease.



# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(prepared in accordance with HKFRS)

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### 2.22 Dividend distribution

Dividend distribution to equity holders of the Company is recognised as a liability in the Group's financial statements in the period in which the dividends are approved by equity holders of the Company.

### 2.23 Government grants

Grants from the government are recognised at their fair value where there is a reasonable assurance that the grant will be received and the Group will comply with all attached conditions.

Government grants relating to costs are deferred and recognised in the income statement over the period necessary to match them with the costs that they are intended to compensate.

Government grants relating to property, plant and equipment are included in non-current liabilities as deferred government grants and are credited to the income statement on a straight-line basis over the expected lives of the related assets.

## 3. FINANCIAL RISK MANAGEMENT

### 3.1 Financial risk factors

The Group's activities expose it to a variety of financial risks: market risk (including currency risk, fair value interest rate risk, cash flow interest rate risk and price risk), credit risk, and liquidity risk. The Group's overall risk management programme focuses on the unpredictability of financial markets and seeks to minimise potential adverse effects on the Group's financial performance.

Risk management is carried out by the Group's finance department (Group Finance) under policies approved by the Board of Directors. Group Finance identifies, evaluates and hedges financial risks in close co-operation with the Group's operating units. The Board provides written principles for overall risk management, as well as written policies covering specific areas, such as foreign exchange risk, interest-rate risk, credit risk and liquidity risk.

- (a) Market risk
  - (i) Foreign exchange risk

The Group is exposed to foreign exchange risk arising from various currency exposures, primarily with respect to United States dollars ("US dollars") and Hong Kong dollars ("HK dollars"). The Group's businesses are principally conducted in RMB, except for import and export of western pharmaceutical products that are mainly conducted in US dollars and HK dollars. Dividend to equity holders of H Shares are declared in RMB and paid in HK dollars. As at 31 December 2006, all of the Group's assets and liabilities were denominated in RMB except that bank and cash balances of RMB20,617,000 (2005:RMB12,749,000), trade and other receivables of RMB11,635,000 (2005: RMB15,651,000) and trade and other payables of RMB40,224,000 (2005: RMB41,605,000) were denominated in US dollars and HK dollars. Foreign exchange risk arises from such future commercial transactions, recognised assets and liabilities and declared dividends could affect the Group's results of operations.

The Group closely monitors trend of exchange rates and its impact on the Group's exchange risk exposure. The Group currently does not have any exchange rate swap arrangement but will consider hedging exchange rate risk should it be arisen.





# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(prepared in accordance with HKFRS)

## 3. FINANCIAL RISK MANAGEMENT (Continued)

### 3.1 Financial risk factors (Continued)

(a) Market risk (Continued)

(ii) Price risk

The Group is exposed to equity securities price risk and investment properties price risk because investments held by the Group are classified on the consolidated balance sheet either as available-for-sale, at fair value through profit or loss or investment properties.

To manage its price risk arising from investments in equity securities, the Group diversifies its portfolio. To manage its price risk arising from investment properties, the Group signs long contracts with lessees.

(iii) Cash flow and fair value interest rate risk

As the Group has no significant interest-bearing assets, the Group's income and operating cash flows are substantially independent of changes in market interest rates.

The Group's interest-rate risk arises from borrowings, details of which have been disclosed in Note 20. All of the Group's borrowings were at fixed rates. As most of the Group's borrowings are current with short maturities of less than one year, exposure to fair value interest rate risk is limited.

(b) Credit risk

The carrying amounts of cash and bank balances, trade and other receivables except for prepayments, available-for-sale financial assets and financial assets at fair value through profit and loss, represent the Group's maximum exposure to credit risk in relation to financial assets. The Group has no significant concentrations of credit risk. It has policies in place to ensure the wholesale sales of products are made to customers with an appropriate credit history. Sales to retail customers are made in cash or via major credit cards.

(c) Liquidity risk

Prudent liquidity risk management implies maintaining sufficient cash, the availability of funding through an adequate amount of committed credit facilities. Due to the dynamic nature of the underlying businesses, the Group aims to maintain flexibility in funding by arranging banking facilities.



# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(prepared in accordance with HKFRS)

## 3. FINANCIAL RISK MANAGEMENT (Continued)

### 3.2 Fair value estimation

The fair value of financial instruments traded in active markets is based on quoted market prices at the balance sheet date.

The fair value of financial instrument that are not traded in an active market is determined by using valuation techniques. The Group uses a variety of methods and makes assumptions that are based on market conditions existing at the balance sheet date. Quoted market prices or dealer quotes for similar instruments are used for long-term debt. Other techniques, such as estimated discounted cash flows, are used to determine fair value for the remaining financial instruments.

The carrying amounts of the Group's financial assets including bank and cash balances, trade and other receivables, available-for-sale financial assets, financial assets at fair value through profit or loss; and financial liabilities including trade and other payables, short-term borrowings, approximate their fair value due to their short maturities. The face values less any estimated credit adjustments for financial assets and liabilities with a maturity of less than one year are assumed to approximate their fair values. The fair value of financial liabilities for disclosure purposes is estimated by discounting the future contractual cash flows at the current market interest rate that is available to the Group for similar financial instruments.

## 4. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS

The Group makes estimates and assumptions concerning the future. The resulting accounting estimates will, by definition, seldom equal the related actual results. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below.

### (a) Useful lives of property, plant, and equipment

The Group's management determines the estimated useful lives and related depreciation charges for its property, plant, and equipment. This estimate is based on the historical experience of the actual useful lives of assets of similar nature and functions. It could change significantly as a result of technical innovations and competitor actions in response to severe industry cycles. Management will increase the depreciation charge where useful lives are less than previously estimated lives, or it will write-off or write-down technically obsolete or non-strategic assets that have been abandoned or sold.

### (b) Net realisable value of inventories

Net realisable value of inventories is the estimated selling price in the ordinary course of business, less estimated costs of completion and selling expenses. These estimates are based on the current market condition and the historical experience and selling goods of similar nature. It could change significantly as a result of change in market condition. Management will reassess the estimations at the balance sheet date.

### (c) Provision for impairment of receivables

The Group's management determines the provision for impairment of receivables. This estimate is based on the credit history of its customers and the current market condition. It could change significantly as a result of change in financial positions of customers. Management will reassess the provision at the balance sheet date.



# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(prepared in accordance with HKFRS)

## 4. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS (Continued)

### (d) Fair value of financial instruments

The fair value of financial instruments that are not traded in an active market is determined by using valuation techniques. The Group uses its judgement to select a variety of methods and makes assumptions that are mainly based on market conditions existing at each balance sheet date.

### (e) Fair value of investment property

The best evidence of fair value is current prices in an active market for similar lease and other contracts. In the absence of such information, the Group determines the amount within the range of reasonable fair value estimates. In making its judgement, the Group considers information from a variety of sources including:

- i) Current prices in an active market for properties of different nature, condition or location (or subject to different lease or other contracts), adjusted to reflect those differences;
- ii) Recent prices of similar properties in less active markets, with adjustments to reflect an changes in economic conditions since the date of the transactions that occurred at those prices; and;
- iii) Discounted cash flow projection based on reliable estimates of future cash flows derived from the terms of any existing lease and other contracts, and (where possible) from external evidence such as current market rents for similar properties in the same location and condition, and using discount rates that reflect current market assessments of the uncertainty in the amount and timing of the cash flows.

The Group has estimated fair value of the investment properties base on result from independent and professionally qualified valuers.

### (f) Deferred taxation

Deferred tax assets related to certain temporary difference and tax losses are recognised as management considers it is probable that the future taxable profit will be available against which the temporary difference or tax losses can be utilised. Where the expectation is different from the original estimate, such differences will impact the recognition of deferred tax assets in the period in which such estimate is changed.



# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(prepared in accordance with HKFRS)

## 5. SEGMENT INFORMATION

### Primary reporting format - business segments

At 31 December 2006, the Group is organised into the following business segments:

- Manufacturing of CPM;
- Wholesale of western pharmaceutical products, CPM, Chinese raw medicine and medical apparatus;
- Retail of western pharmaceutical products, CPM, Chinese raw medicine and medical apparatus; and
- Import and export of western pharmaceutical products, CPM and medical apparatus.

Turnover consists of sales of goods from the above business segments, which are RMB10,241,004,000 and RMB9,026,340,000 for the years ended 31 December 2006 and 2005 respectively.

Other operations of the Group mainly comprise holding of investment properties and other investments, neither of which are of a sufficient size to be separately reported.

The segment results are as follows:

	Year ended 31 December 2006					
	Manufacturing RMB'000	Wholesale RMB'000	Retail RMB'000	Import and export RMB'000	Elimination RMB'000	Group RMB'000
<b>Total gross segment sales</b>	2,452,074	8,449,687	336,468	279,795	(1,277,020)	10,241,004
Inter-segment sales	(39,890)	(1,182,314)	(596)	(54,220)	1,277,020	—
Sales	<u>2,412,184</u>	<u>7,267,373</u>	<u>335,872</u>	<u>225,575</u>	<u>—</u>	<u>10,241,004</u>
Segment results	296,403	138,037	9,427	6,319	(42,460)	407,546
Unallocated cost						(12,752)
Operating profit						394,794
Finance costs (Note 26)						(45,360)
Share of losses of associates (Note 11)	(279)					(279)
<b>Profit before income tax</b>						349,155
Income tax expense (Note 27)						(118,567)
<b>Profit for the year</b>						<u>230,588</u>



# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(prepared in accordance with HKFRS)

## 5. SEGMENT INFORMATION (Continued)

### Primary reporting format - business segments (Continued)

	Year ended 31 December 2005					
	Manufacturing RMB'000	Wholesale RMB'000	Retail RMB'000	Import and export RMB'000	Elimination RMB'000	Group RMB'000
<b>Total gross segment sales</b>	2,187,677	7,088,324	318,669	265,572	(833,902)	9,026,340
Inter-segment sales	(46,002)	(743,036)	—	(44,864)	833,902	—
Sales	<u>2,141,675</u>	<u>6,345,288</u>	<u>318,669</u>	<u>220,708</u>	<u>—</u>	<u>9,026,340</u>
Segment results	255,701	132,974	3,179	5,206	(27,477)	369,583
Unallocated profit						732
Operating profit						370,315
Finance costs (Note 26)						(53,610)
Share of losses of associates (Note 11)	(1,212)					(1,212)
<b>Profit before income tax</b>						315,493
Income tax expense (Note 27)						(107,771)
<b>Profit for the year</b>						<u>207,722</u>

Other segment items included in the income statement are as follows:

	Year ended 31 December 2006					
	Manufacturing RMB'000	Wholesale RMB'000	Retail RMB'000	Import and export RMB'000	Unallocated RMB'000	Group RMB'000
Depreciation (Note 6)	98,573	21,468	2,626	157	3,809	126,633
Amortisation (Notes 8 and 9)	13,293	5,502	—	—	—	18,795
Impairment of inventories (Note 14)	3,942	—	—	—	—	3,942
Reversal of inventories impairment (Note 14)	—	(643)	(672)	—	—	(1,315)
Impairment of trade and other receivables	3,240	8,893	(45)	796	—	12,884
Reversal of trade and other receivables impairment	(2,083)	—	—	—	—	(2,083)
Impairment of property, plant, and equipment (Note 6)	108	101	—	—	—	209



# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(prepared in accordance with HKFRS)

## 5. SEGMENT INFORMATION (Continued)

### Primary reporting format - business segments (Continued)

	Year ended 31 December 2005					
	Manufacturing	Wholesale	Retail	Import and export	Unallocated	Group
	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000
Depreciation (Note 6)	99,272	19,152	2,113	173	4,679	125,389
Amortisation (Notes 8 and 9)	12,780	4,387	—	—	—	17,167
Impairment of goodwill (Note 9)	507	1,497	—	—	—	2,004
Impairment of inventories (Note 14)	580	929	—	—	—	1,509
Reversal of inventories impairment (Note 14)	—	(4,303)	—	—	—	(4,303)
Impairment of trade and other receivables	2,465	4,456	—	611	—	7,532
Reversal of trade and other receivables impairment	(1,692)	(100)	—	—	—	(1,792)
Reversal of property, plant, and equipment impairment (Note 6)	(341)	—	—	—	(7,110)	(7,451)

The segment assets and liabilities at 31 December 2006 and capital expenditure for the year then ended are as follows:

	Year ended 31 December 2006						
	Manufacturing	Wholesale	Retail	Import and export	Unallocated	Elimination	Group
	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000
Assets	2,609,835	2,781,627	182,883	111,858	605,250	(694,574)	5,596,879
Associates	44,085	—	—	—	—	—	44,085
<b>Total assets</b>	<b>2,653,920</b>	<b>2,781,627</b>	<b>182,883</b>	<b>111,858</b>	<b>605,250</b>	<b>(694,574)</b>	<b>5,640,964</b>
<b>Liabilities</b>	<b>642,373</b>	<b>2,346,688</b>	<b>87,416</b>	<b>86,370</b>	<b>92,311</b>	<b>(694,574)</b>	<b>2,560,584</b>
<b>Capital expenditure (Notes 6, 8 and 9)</b>	<b>86,397</b>	<b>10,222</b>	<b>1,074</b>	<b>491</b>	<b>3,710</b>	<b>—</b>	<b>101,894</b>



# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(prepared in accordance with HKFRS)

## 5. SEGMENT INFORMATION (Continued)

### Primary reporting format - business segments (Continued)

The segment assets and liabilities at 31 December 2005 and capital expenditure for the year then ended are as follows:

	Manufacturing	Wholesale	Retail	Import and export	Unallocated	Elimination	Group
	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000
Assets	2,499,796	2,436,726	194,843	122,651	684,748	(627,198)	5,311,566
Associates	4,854	—	—	—	—	—	4,854
<b>Total assets</b>	<b>2,504,650</b>	<b>2,436,726</b>	<b>194,843</b>	<b>122,651</b>	<b>684,748</b>	<b>(627,198)</b>	<b>5,316,420</b>
<b>Liabilities</b>	<b>643,665</b>	<b>2,086,885</b>	<b>90,904</b>	<b>100,043</b>	<b>97,291</b>	<b>(627,198)</b>	<b>2,391,590</b>
<b>Capital expenditure (Notes 6, 8 and 9)</b>	<b>112,071</b>	<b>19,116</b>	<b>5,178</b>	<b>60</b>	<b>843</b>	<b>—</b>	<b>137,268</b>

Inter-segment transfers or transactions are entered into under the normal commercial terms and conditions that would also be available to unrelated third parties.

Segment assets consist primarily of land use rights, property, plant and equipment, intangible assets, investments in associates, inventories, trade and other receivables, and bank and cash balances. Unallocated assets comprise deferred taxation, investment properties, available-for-sale financial assets, other financial assets at fair value through profit or loss and corporate assets.

Segment liabilities comprise operating liabilities. Unallocated liabilities comprise items such as taxation and certain corporate liabilities.

Capital expenditure comprises additions to land use rights (Note 8), property, plant and equipment (Note 6) and intangible assets (Note 9).

### Secondary reporting format - geographical segments

No geographical segments are presented as sales and results attributable to the markets outside the PRC are not more than 10% of the Group's consolidated sales and consolidated results.



# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(prepared in accordance with HKFRS)

## 6. PROPERTY, PLANT AND EQUIPMENT

### Group

	Plant and buildings RMB'000	Machinery and equipment RMB'000	Motor vehicles RMB'000	Construction in progress RMB'000	Total RMB'000
<b>At 1 January 2005</b>					
Cost	1,145,041	927,987	83,671	108,519	2,265,218
Accumulated depreciation	(243,540)	(352,159)	(54,810)	—	(650,509)
Accumulated impairment	(18,119)	(6,764)	(471)	—	(25,354)
Net book amount	<u>883,382</u>	<u>569,064</u>	<u>28,390</u>	<u>108,519</u>	<u>1,589,355</u>
<b>Year ended 31 December 2005</b>					
Opening net book amount	883,382	569,064	28,390	108,519	1,589,355
Additions	10,370	25,666	3,088	90,619	129,743
Transfers	17,749	30,465	1,204	(49,418)	—
Disposals (Note 31)	(748)	(4,020)	(534)	—	(5,302)
Disposal of a subsidiary	—	(3,333)	—	—	(3,333)
Impact arising from dilution of equity interest in a subsidiary (the subsidiary became a jointly controlled entity subsequent to the dilution)	(35,638)	(12,128)	(1,755)	(936)	(50,457)
Depreciation (Note 24)	(50,709)	(67,557)	(7,123)	—	(125,389)
Reversal of impairment charge (Note 5)	7,110	245	96	—	7,451
Closing net book amount	<u>831,516</u>	<u>538,402</u>	<u>23,366</u>	<u>148,784</u>	<u>1,542,068</u>
<b>At 31 December 2005</b>					
Cost	1,132,693	935,531	80,104	148,784	2,297,112
Accumulated depreciation	(290,168)	(390,610)	(56,363)	—	(737,141)
Accumulated impairment	(11,009)	(6,519)	(375)	—	(17,903)
Net book amount	<u>831,516</u>	<u>538,402</u>	<u>23,366</u>	<u>148,784</u>	<u>1,542,068</u>
<b>Year ended 31 December 2006</b>					
Opening net book amount	831,516	538,402	23,366	148,784	1,542,068
Additions	7,077	18,427	2,930	69,157	97,591
Transfers	63,966	24,411	729	(89,106)	—
Transfers to investment properties (Note 7)	(8,213)	—	—	—	(8,213)
Transfers to intangible assets (Note 9)	—	—	—	(2,590)	(2,590)
Disposals (Note 31)	(5,055)	(2,668)	(503)	—	(8,226)
Investment in an associate	(10,758)	(1,923)	—	(2,845)	(15,526)
Depreciation (Note 24)	(53,153)	(67,439)	(6,041)	—	(126,633)
Impairment charge (Note 5)	—	(108)	(101)	—	(209)
Closing net book amount	<u>825,380</u>	<u>509,102</u>	<u>20,380</u>	<u>123,400</u>	<u>1,478,262</u>
<b>At 31 December 2006</b>					
Cost	1,159,923	913,769	79,920	123,530	2,277,142
Accumulated depreciation	(323,630)	(398,948)	(59,180)	—	(781,758)
Accumulated impairment	(10,913)	(5,719)	(360)	(130)	(17,122)
Net book amount	<u>825,380</u>	<u>509,102</u>	<u>20,380</u>	<u>123,400</u>	<u>1,478,262</u>





# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(prepared in accordance with HKFRS)

## 6. PROPERTY, PLANT AND EQUIPMENT (Continued)

Impairment charge mainly resulted from as a result of modernisation of production facilities. Reversal of impairment charge is due to the increase in market value of the assets. Impairment charge and reversal of impairment charge are included in administrative expenses in the income statement.

Depreciation of RMB79,913,000 (2005: RMB80,470,000) has been expensed in cost of goods sold, RMB Nil (2005: RMB80,000) in selling and marketing costs and RMB46,720,000 (2005: RMB44,839,000) in administrative expenses.

Lease rental expenses amounting to RMB33,034,000 (2005: RMB33,377,000) relating to the lease of properties, are included in the income statement (Note 24).

All of the Group's buildings are located in the PRC, except for a property with net book amount of RMB15,132,342 (2005: RMB15,679,000) located in Hong Kong.

Certain property, plant and equipment of the Group with net book amounts totalling RMB54,970,000 (2005: RMB93,511,000) have been pledged for securing bank borrowings of the Group (Note 20).

### Company



	Plant and buildings <i>RMB'000</i>	Machinery and equipment <i>RMB'000</i>	Motor vehicles <i>RMB'000</i>	Total <i>RMB'000</i>
<b>At 1 January 2005</b>				
Cost	25,055	19,508	1,530	46,093
Accumulated depreciation	(6,832)	(9,752)	(450)	(17,034)
Accumulated impairment	(7,110)	—	—	(7,110)
Net book amount	<u>11,113</u>	<u>9,756</u>	<u>1,080</u>	<u>21,949</u>
<b>Year ended 31 December 2005</b>				
Opening net book amount	11,113	9,756	1,080	21,949
Additions	—	263	—	263
Disposals	—	(30)	—	(30)
Depreciation	(1,614)	(2,914)	(151)	(4,679)
Reversal of impairment charge	7,110	—	—	7,110
Closing net book amount	<u>16,609</u>	<u>7,075</u>	<u>929</u>	<u>24,613</u>
<b>At 31 December 2005</b>				
Cost	25,055	19,740	1,530	46,325
Accumulated depreciation	(8,446)	(12,665)	(601)	(21,712)
Net book amount	<u>16,609</u>	<u>7,075</u>	<u>929</u>	<u>24,613</u>

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(prepared in accordance with HKFRS)

## 6. PROPERTY, PLANT AND EQUIPMENT (Continued)

### Company (Continued)

	Plant and buildings RMB'000	Machinery and equipment RMB'000	Motor vehicles RMB'000	Total RMB'000
<b>Year ended 31 December 2006</b>				
Opening net book amount	16,609	7,075	929	24,613
Additions	—	812	263	1,075
Disposals	—	(20)	—	(20)
Depreciation	(965)	(2,701)	(170)	(3,836)
Closing net book amount	<u>15,644</u>	<u>5,166</u>	<u>1,022</u>	<u>21,832</u>
<b>At 31 December 2006</b>				
Cost	25,058	20,425	1,793	47,276
Accumulated depreciation	( 9,414)	(15,259)	(771)	(25,444)
Net book amount	<u>15,644</u>	<u>5,166</u>	<u>1,022</u>	<u>21,832</u>

Depreciation of RMB3,836,000 (2005: RMB4,679,000) has been expensed in administrative expenses.

Lease rental expenses amounting to RMB1,093,000 (2005: RMB1,235,000) relating to the lease of properties are included in the income statement.

## 7. INVESTMENT PROPERTIES - GROUP

	2006 RMB'000	2005 RMB'000
At 1 January	8,712	8,712
Transfers from owner-occupied properties (Note 6)	8,213	—
Transfers from land use rights (Note 8)	3,866	—
Fair value gains - included in equity (Note 18)	14,634	—
Change of fair value in investment properties	(12)	—
At 31 December	<u>35,413</u>	<u>8,712</u>

The Group's investment properties are located in the PRC and were revalued either by Greater China Appraisal Limited or Guangdong Yangcheng Certified Public Accountants Co., Ltd., independent and professionally qualified valuers, at 31 December 2006. Except for a property revalued at its industrial use based on depreciated replacement cost method, other properties were revalued based on discounted cash flow method.



# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(prepared in accordance with HKFRS)

## 8. LAND USE RIGHTS - GROUP

The Group's interests in land use rights represent prepaid operating lease payments on leases of between 20 years to 50 years in the PRC. The land use rights with net book value are analysed as follows:

	2006 RMB'000	2005 RMB'000
Opening	134,691	140,202
Additions	2,788	—
Impact arising from dilution of equity interest in a subsidiary (the subsidiary became a jointly controlled entity subsequent to the dilution)	—	(1,529)
Amortisation (Note 24)	(5,813)	(3,982)
Transfers to investment properties (Note 7)	(3,866)	—
	<u>127,800</u>	<u>134,691</u>

## 9. INTANGIBLE ASSETS

### Group

	Goodwill RMB'000	Patent and trademarks RMB'000	Staff quarters reform costs RMB'000	Software RMB'000	Total RMB'000
<b>At 1 January 2005</b>					
Cost	2,154	7,988	104,467	—	114,609
Accumulated amortisation	(150)	(571)	(56,342)	—	(57,063)
Net book amount	<u>2,004</u>	<u>7,417</u>	<u>48,125</u>	<u>—</u>	<u>57,546</u>
<b>Year ended 31 December 2005</b>					
Opening net book amount	2,004	7,417	48,125	—	57,546
Additions	—	500	—	7,025	7,525
Impact arising from dilution of equity interest in a subsidiary (the subsidiary became a jointly controlled entity subsequent to the dilution)	—	—	(376)	—	(376)
Impairment charge (Note 24)	(2,004)	—	—	—	(2,004)
Amortisation (Note 24)	—	(932)	(10,382)	(1,871)	(13,185)
Closing net book amount	<u>—</u>	<u>6,985</u>	<u>37,367</u>	<u>5,154</u>	<u>49,506</u>
<b>At 31 December 2005</b>					
Cost	2,154	8,488	104,092	7,025	121,759
Accumulated amortisation	(150)	(1,503)	(66,725)	(1,871)	(70,249)
Accumulated impairment	(2,004)	—	—	—	(2,004)
Net book amount	<u>—</u>	<u>6,985</u>	<u>37,367</u>	<u>5,154</u>	<u>49,506</u>



# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(prepared in accordance with HKFRS)

## 9. INTANGIBLE ASSETS (Continued)

### Group (Continued)

	Goodwill RMB'000	Patent and trademarks RMB'000	Staff quarters reform costs RMB'000	Software RMB'000	Total RMB'000
<b>Year ended 31 December 2006</b>					
Opening net book amount	—	6,985	37,367	5,154	49,506
Additions	—	190	—	1,325	1,515
Transfers from construction in progress (Note 6)	—	—	—	2,590	2,590
Amortisation (Note 24)	—	(870)	(10,361)	(1,751)	(12,982)
Closing net book amount	—	6,305	27,006	7,318	40,629
<b>At 31 December 2006</b>					
Cost	2,154	8,678	104,092	10,940	125,864
Accumulated amortisation	(150)	(2,373)	(77,086)	(3,622)	(83,231)
Accumulated impairment	(2,004)	—	—	—	(2,004)
Net book amount	—	6,305	27,006	7,318	40,629

### Company

	2006 RMB'000	2005 RMB'000
<b>Staff quarters reform costs</b>		
<b>At 1 January</b>		
Cost	2,524	2,524
Accumulated amortisation	(1,552)	(1,309)
Net book amount	972	1,215
<b>Year ended 31 December</b>		
Opening net book amount	972	1,215
Amortisation	(243)	(243)
Closing net book amount	729	972
<b>At 31 December</b>		
Cost	2,524	2,524
Accumulated amortisation	(1,795)	(1,552)
Net book amount	729	972

Amortisation has been included in administrative expenses in the income statement.

The carrying amount of the unit has been reduced to its recoverable amount through recognition of an impairment loss against goodwill. This loss has been included in administrative expenses in the income statement.



# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(prepared in accordance with HKFRS)

## 10. INVESTMENTS IN SUBSIDIARIES — COMPANY

	2006 RMB'000	2005 RMB'000
Investments in subsidiaries — unlisted equity securities, at cost	1,413,712	1,612,895
Add: Additions	46,414	—
Less: Provision for impairment losses	—	(97,148)
Less: Impact arising from dilution of equity interest in a subsidiary (the subsidiary became a jointly controlled entity subsequent to the dilution)	—	(102,035)
	<u>1,460,126</u>	<u>1,413,712</u>

Particulars of the principal subsidiaries are set out in Note 34.

## 11. INVESTMENTS IN ASSOCIATES

### Group

	2006 RMB'000	2005 RMB'000
<b>At 1 January</b>	<b>4,854</b>	<b>6,066</b>
Additions	41,280	—
Disposals	(1,770)	—
Share of losses of associates	(279)	(1,212)
	<u>44,085</u>	<u>4,854</u>

The Group's investments in its associates, all of which are unlisted, were as follows:

Name	Particulars of issued capital held	Country of incorporation	Principal activities	Interest held	
				2006 %	2005 %
Guangzhou Zhong Fu Medical Co., Ltd.	Registered capital: RMB0.8 million	PRC	Production of CPM	—	50.00
Ming Tai Enterprises (Thailand) Ltd.	Ordinary shares of Baht1 each	Thailand	Dormant	—	40.00
Guangzhou Jinshen Medical Co., Ltd.	Registered capital: RMB1.5 million	PRC	Production of health medicine	38.25	38.25
Guangzhou Jihua Bio-chemical Co., Ltd.	Registered capital: RMB10 million	PRC	Development, manufacture and sales of medical apparatus and instruments	24.00	24.00
Shanghai Jiuhe Tang Chinese Medicine Co., Ltd.	Registered capital: RMB1.9 million	PRC	Sales of Chinese medicine	29.72	29.72
Guangzhou Pharmaceutical Soccer Club Limited	Registered capital: RMB20 million	PRC	Participation of soccer competition and provision of related advertising services	50.00	—
Guangzhou Nuo Cheng Bio-product Co., Ltd.	Registered capital: RMB64 million	PRC	Manufacture and sales of bio-product	50.00	—



# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(prepared in accordance with HKFRS)

## 11. INVESTMENTS IN ASSOCIATES (Continued)

### Group (continued)

The aggregated amounts of assets and liabilities as at 31 December 2006 and aggregated revenues and net losses for the year then ended of the Group's associates were as follows:

	2006 RMB'000	2005 RMB'000
Assets	96,851	41,689
Liabilities	33,748	30,178
Revenues	89,694	86,084
Net losses	<u>(1,048)</u>	<u>(1,628)</u>

### Company

	2006 RMB'000	2005 RMB'000
Investments in associates		
— Unlisted equity securities, at cost	<u>2,120</u>	<u>2,179</u>

## 12 INVESTMENTS IN JOINTLY CONTROLLED ENTITIES

### Group

The Group's investments in its jointly controlled entities, all of which are unlisted, were as follows:

Name	Particulars of issued capital held	Country of incorporation	Principal activities	Interest held	
				2006 %	2005 %
Guangzhou Wao Lao Ji Pharmaceutical Co., Ltd.	Registered capital: RMB204,756,878	PRC	Production of CPM	48.05	48.05
Guangzhou Lianjie Computer Technology Co., Ltd.	Registered capital: RMB500,000	PRC	Provision of enterprise resources planning consultation services	50.00	50.00
PT. Purusa Bhakti	Ordinary shares of US\$1 each	Indonesia	Dormant	50.00	50.00



# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(prepared in accordance with HKFRS)

## 12 INVESTMENTS IN JOINTLY CONTROLLED ENTITIES (Continued)

### Group (continued)

The following amounts represent the Group's share of assets, liabilities, and results of these jointly controlled entities that have been included in the consolidated balance sheet and consolidated income statement respectively:

	2006 RMB'000	2005 RMB'000
<b>Assets:</b>		
Non-current assets	67,134	61,069
Current assets	148,220	140,566
	<u>215,354</u>	<u>201,635</u>
<b>Liabilities:</b>		
Non-current liabilities	4,124	4,547
Current liabilities	26,100	24,592
	<u>30,224</u>	<u>29,139</u>
<b>Net assets</b>	<u>185,130</u>	<u>172,496</u>
<b>Results:</b>		
Income	318,041	245,431
Expenses	(286,615)	(216,598)
Profit after income tax	<u>31,426</u>	<u>28,833</u>
Proportionate interest in commitments	<u>785</u>	<u>38,722</u>

There are no contingent liabilities relating to the Group's investments in these jointly controlled entities, and no contingent liabilities of these entities themselves.

### Company

	2006 RMB'000	2005 RMB'000
Investments in jointly controlled entities:		
— Unlisted equity securities, at cost	<u>102,035</u>	<u>102,035</u>

## 13. AVAILABLE-FOR-SALE FINANCIAL ASSETS

	Group		Company	
	2006 RMB'000	2005 RMB'000	2006 RMB'000	2005 RMB'000
At 1 January	61,994	64,863	58,683	64,739
Additions	—	363	—	200
Disposals	(30,000)	(1,139)	(30,000)	—
Impairment charge (Note 24)	(1,769)	(2,093)	(1,395)	(6,256)
At 31 December	<u>30,225</u>	<u>61,994</u>	<u>27,288</u>	<u>58,683</u>

Available-for-sale financial assets are unlisted equity securities. Impairment charge, recognised due to the decline in fair value of financial assets below their carrying amounts, has been included in administrative expenses in the income statement.

The fair value of unlisted securities is estimated based on the net assets of the target company and its recoverability.



# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(prepared in accordance with HKFRS)

## 14. INVENTORIES

	Group		Company	
	2006 RMB'000	2005 RMB'000	2006 RMB'000	2005 RMB'000
Raw materials	154,897	116,937	—	—
Work in progress	91,019	110,260	—	—
Finished goods	134,026	91,550	—	—
Merchandise	938,077	828,982	9,974	—
Production supplies	8,425	840	—	—
	<b>1,326,444</b>	<b>1,148,569</b>	<b>9,974</b>	<b>—</b>

The cost of inventories recognised as expense including those in cost of goods sold, amounted to RMB8,474,855,000 (2005: RMB7,470,180,000).

During the year ended 31 December 2006, the Group has recognised impairment charge amounting to RMB3,942,000 (2005: RMB1,509,000) based on the difference between estimated net realisable value and net book value of such inventories. The amount has been included in administrative expenses in the income statement.

The Group reversed RMB1,315,000 (2005: RMB4,303,000) of a previous inventory write-down during the year ended 31 December 2006 based on the sales proceeds of such inventories. The amount reversed has been included in administrative expenses in the income statement.



## 15. TRADE AND OTHER RECEIVABLES

	Group		Company	
	2006 RMB'000	2005 RMB'000	2006 RMB'000	2005 RMB'000
Trade receivables (a)	1,401,804	1,004,658	26,229	—
Less: provision for impairment of receivables (b)	(45,362)	(44,881)	(262)	—
Trade receivables — net	1,356,442	959,777	25,967	—
Bills receivable	380,010	331,754	241	—
Other receivables and prepayments	263,503	386,606	7,696	710
Due from				
Subsidiaries (c)	—	—	625,018	522,665
Ultimate holding company (d)	4,071	5,060	3,792	5,555
Dividends receivable from subsidiaries	—	—	135,964	109,490
	<b>2,004,026</b>	<b>1,683,197</b>	<b>798,678</b>	<b>638,420</b>

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# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(prepared in accordance with HKFRS)

## 15. TRADE AND OTHER RECEIVABLES (Continued)

Note:

- (a) Trade receivables generated from credit sales generally have credit terms of one to three months. The ageing analysis of trade receivables is as follows:

	Group		Company	
	2006 RMB'000	2005 RMB'000	2006 RMB'000	2005 RMB'000
Within 6 months	1,306,538	922,280	26,229	—
6 months to 1 year	51,497	24,949	—	—
Over 1 year	43,769	57,429	—	—
	<b>1,401,804</b>	<b>1,004,658</b>	<b>26,229</b>	<b>—</b>

At 31 December 2006, trade receivables amounted to RMB139,613,000 (2005: RMB260,821,000) were discounted by enterprises in the Group to banks in the PRC with recourse. The corresponding collateralised borrowings were included in short-term bank borrowings.

There is no concentration of credit risk with respect to trade receivables as the Group has a large number of customers widely dispersed within the PRC.

- (b) Movements on provision for impairment of receivables are as follows:

	Group		Company	
	2006 RMB'000	2005 RMB'000	2006 RMB'000	2005 RMB'000
At 1 January	44,881	54,457	—	—
Impairment charge	8,888	427	262	—
Receivables written-offs	(8,407)	(10,003)	—	—
At 31 December	<b>45,362</b>	<b>44,881</b>	<b>262</b>	<b>—</b>

The creation of provision for impaired receivables has been included in administrative expenses in the income statement.

- (c) The amounts due are unsecured, interest bearing at commercial market rate and repayable on demand.  
 (d) The amounts due are unsecured, interest free and repayable on demand.

## 16. BANK AND CASH BALANCES

	Group		Company	
	2006 RMB'000	2005 RMB'000	2006 RMB'000	2005 RMB'000
Cash at bank and in hand	417,316	454,808	4,762	63,264
Short-term deposits	71,812	163,773	59,969	26,839
	<b>489,128</b>	<b>618,581</b>	<b>64,731</b>	<b>90,103</b>

Cash at bank earned interests at floating rates based on daily bank deposit balances. As at 31 December 2006, maturity of short-term deposits varied from seven days to three months, depending on the cash requirements of the Group. Bank deposits earned interests at the short-term deposit rates, the effective interest rate of which ranges from 1.62% to 1.80% (2005: 1.62% to 1.80%).



# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(prepared in accordance with HKFRS)

## 17. SHARE CAPITAL

	As at 31 December 2005		Transfers(from)/to		As at 31 December 2006	
	No. of shares	Amount RMB'000	No. of shares	Amount RMB'000	No. of shares	Amount RMB'000
<b>Share capital registered, issued and fully paid of RMB1 each</b>						
Non-circulating state shares	513,000,000	513,000	(513,000,000)	(513,000)	—	—
Circulating state shares subject to exchange restrictions	—	—	489,600,000	489,600	489,600,000	489,600
H shares	219,900,000	219,900	—	—	219,900,000	219,900
A shares	78,000,000	78,000	23,400,000	23,400	101,400,000	101,400
	<u>810,900,000</u>	<u>810,900</u>	<u>—</u>	<u>—</u>	<u>810,900,000</u>	<u>810,900</u>
Share premium on issue of shares net of issuing expenses		781,134		—		781,134
<b>Total</b>		<u>1,592,034</u>		<u>—</u>		<u>1,592,034</u>

Pursuant to the rules and regulations issued by the relevant PRC authorities, and the agreements reached between the equity holders of the non-circulating state shares and the equity holders of A shares on 12 April 2006, the equity holders of the non-circulating state shares transferred 3 shares for every 10 shares to the equity holders of A shares. Following the transfer, the non-circulating state shares became circulating state shares which are subject to certain exchange restrictions.



## 18. OTHER RESERVES

	Group				Total
	Capital reserve (Note a) RMB'000	Statutory surplus reserve (Note b) RMB'000	Statutory public welfare fund (Note b) RMB'000	Discretionary surplus reserve (Note b) RMB'000	
<b>At 1 January 2005</b>	399,832	218,022	153,573	109,000	880,427
Transfers from retained earnings, net	1,966	38,563	34,119	24,036	98,684
Impact arising from dilution of equity interest in a subsidiary (the subsidiary became a jointly controlled entity subsequent to the dilution)	19,819	(3,455)	(3,006)	(3,455)	9,903
<b>At 31 December 2005</b>	<u>421,617</u>	<u>253,130</u>	<u>184,686</u>	<u>129,581</u>	<u>989,014</u>
<b>At 1 January 2006</b>	421,617	253,130	184,686	129,581	989,014
Transfers from retained earnings, net	2,690	45,412	—	35,408	83,510
Revaluation of investment property	13,116	—	—	—	13,116
Transfers	—	184,686	(184,686)	—	—
Disposal of a subsidiary	—	(154)	—	—	(154)
<b>At 31 December 2006</b>	<u>437,423</u>	<u>483,074</u>	<u>—</u>	<u>164,989</u>	<u>1,085,486</u>

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(prepared in accordance with HKFRS)

## 18. OTHER RESERVES (Continued)

	Company			Total RMB'000
	Capital reserve RMB'000	Statutory surplus reserve (note b) RMB'000	Statutory public welfare fund (note b) RMB'000	
<b>At 1 January 2005</b>	397,924	91,503	61,615	551,042
Transfers from retained earnings, net	100	19,314	9,657	29,071
<b>At 31 December 2005</b>	<u>398,024</u>	<u>110,817</u>	<u>71,272</u>	<u>580,113</u>
<b>At 1 January 2006</b>	398,024	110,817	71,272	580,113
Transfers	—	71,272	(71,272)	—
Transfers from retained earnings, net	100	24,237	—	24,337
<b>At 31 December 2006</b>	<u>398,124</u>	<u>206,326</u>	<u>—</u>	<u>604,450</u>

### (a) Capital reserve

Transfers from retained earnings included:

- an amount of RMB1,198,000 (2005: RMB452,000) represented deferred income on government grants, after deducting minority interest.
- an amount of RMB2,498,000 (2005: RMB2,397,000) represented waiver of debts, after deducting minority interest.
- an amount of RMB91,000 (2005: RMB440,000) represented donations received, after deducting minority interest.
- an amount of RMB238,000 (2005: Nil) represented negative goodwill arising from investment in an associate with assets contributed by a subsidiary.
- an amount of RMB13,116,000 (2005: Nil) represented the difference between the fair value and the carrying amount of the assets on the date when the use of the assets changed from owner-occupied assets to investment properties, after deducting minority interest.
- in 2005, an amount of RMB19,819,000 represented income arising from dilution of equity interest in a subsidiary.

Transfers to retained earnings included:

- an amount of RMB1,323,000 (2005: RMB1,323,000) represented depreciation on revalued fixed assets, net of deferred tax credits.
- an amount of RMB12,000 (2005: Nil) represented change of fair value in investment properties.

Upon approval from the Board of Directors, capital surplus, other than those relating to receipts of donated non-cash assets and equity investments held, can be used to increase capital. Capital surplus arising from receipts of donated non-cash assets and equity investments can only be used to increase capital after the donated assets or investments have been disposed of.



# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(prepared in accordance with HKFRS)

## 18. OTHER RESERVES (Continued)

### (b) Surplus reserve

The Company, its subsidiaries, jointly controlled entities and associates established in the PRC ("PRC Companies") are required to maintain certain surplus reserves by transferring from their profit after income tax in accordance with the relevant laws and regulations and, if applicable, Articles of Association, before any dividend is declared and paid.

#### Statutory surplus reserve

The PRC companies are required to transfer 10% of their profit after income tax calculated in accordance with the PRC accounting standards and systems, to the statutory surplus reserve until the balance reaches 50% of their respective registered capital, where further transfers will be at their directors' recommendation. The statutory surplus reserve can only be used to make up prior years' losses or to increase share capital.

#### Statutory public welfare fund

Pursuant to the amendment to the Company Law in the PRC effective 1 January 2006, the PRC companies are not required to provide statutory public welfare fund. According to the relevant accounting regulations, these companies have transferred the balances of statutory public welfare fund to statutory surplus reserve since 1 January 2006.

#### Discretionary surplus reserve

In accordance with relevant PRC regulations and subject to approval by shareholders in general meeting, discretionary surplus reserve fund can be used to reduce any losses incurred, to increase share capital or to pay dividends.



## 19. TRADE AND OTHER PAYABLES

	Group		Company	
	2006 RMB'000	2005 RMB'000	2006 RMB'000	2005 RMB'000
Trade payables (a)	1,067,798	955,704	22,722	—
Due to				
Subsidiaries (b)	—	—	11,343	42,444
Ultimate holding company (b)	16,994	25,468	—	—
Other payables and accrued charges	453,108	378,548	8,034	12,323
	<u>1,537,900</u>	<u>1,359,720</u>	<u>42,099</u>	<u>54,767</u>

### (a) The ageing analysis of trade payables as at 31 December 2006 is as follows:

	Group		Company	
	2006 RMB'000	2005 RMB'000	2006 RMB'000	2005 RMB'000
Within 1 year	1,019,514	908,119	22,722	—
1 year to 2 years	25,241	25,264	—	—
Over 2 years	23,043	22,321	—	—
	<u>1,067,798</u>	<u>955,704</u>	<u>22,722</u>	<u>—</u>

### (b) The amounts due are unsecured, interest free and repayable on demand.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(prepared in accordance with HKFRS)

## 20. BORROWINGS

	Group		Company	
	2006 RMB'000	2005 RMB'000	2006 RMB'000	2005 RMB'000
<b>Current</b>				
Short-term bank borrowings				
— secured	30,000	43,961	—	—
Short-term bank borrowings				
— unsecured	858,199	823,824	30,000	—
Current portion of long-term bank borrowings - unsecured	—	50,000	—	—
	<b>888,199</b>	<b>917,785</b>	<b>30,000</b>	<b>—</b>

All bank borrowings are bearing interest at prevailing market rates. Bank borrowings have been secured by property, plant and equipment of the Group with carrying value of RMB54,970,000 as at 31 December 2006 (2005: RMB93,511,000) (Note 6).

The repayment terms of borrowings were as follows:

	Group		Company	
	2006 RMB'000	2005 RMB'000	2006 RMB'000	2005 RMB'000
Within 1 year	<b>888,199</b>	<b>917,785</b>	<b>30,000</b>	<b>—</b>

The effective interest rates at the balance sheet date were as follows:

	2006	2005
Short-term bank borrowings	<b>5.347%</b>	<b>5.236%</b>

The carrying amounts of short-term borrowings approximate their fair value.

The carrying amounts of all the Group's borrowings are denominated in RMB.

The Group has the following undrawn borrowing facilities:

	2006 RMB'000	2005 RMB'000
Floating rate		
— expiring within one year	<b>23,976</b>	<b>25,671</b>



# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(prepared in accordance with HKFRS)

## 21. DEFERRED INCOME TAX

Deferred income tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets against current tax liabilities and when the deferred income taxes relate to the same fiscal authority. The Group did not have such offset amount as at 31 December 2006 (2005: Nil).

	Group		Company	
	2006 RMB'000	2005 RMB'000	2006 RMB'000	2005 RMB'000
Deferred income tax assets:				
— Deferred income tax assets to be recovered within 12 months	17,950	—	—	—
— Deferred income tax assets to be recovered after more than 12 months	47,002	53,345	4,687	—
	<b>64,952</b>	<b>53,345</b>	<b>4,687</b>	<b>—</b>

In accordance with the PRC tax law or other tax regulations applicable to those companies in their respective jurisdictions, tax losses may be carried forward against future taxable income. The Group did not recognise deferred tax assets of RMB27,777,000 (2005: RMB19,873,000) in respect of tax losses amounting to RMB84,172,000 (2005: RMB60,220,000), as management believes it is more likely than not that such tax losses would not be realised before they expire. Losses amounting to RMB Nil, RMB3,135,000, RMB31,654,000, RMB25,431,000 and RMB23,952,000 will expire in 2007, 2008, 2009, 2010 and 2011, respectively.

	Group	
	2006 RMB'000	2005 RMB'000
Deferred income tax liabilities:		
— Deferred income tax liabilities to be settled within 12 months	652	—
— Deferred income tax liabilities to be settled after more than 12 months	41,218	42,522
	<b>41,870</b>	<b>42,522</b>

The Company did not have deferred income tax liabilities as at 31 December 2006 (2005: Nil).

The gross movement on the deferred income tax account is as follows:

	Group		Company	
	2006 RMB'000	2005 RMB'000	2006 RMB'000	2005 RMB'000
Beginning of the year	(10,823)	(5,981)	—	—
Recognised in the income statement (Note 27)	(12,259)	(4,842)	(4,687)	—
End of the year	<b>(23,082)</b>	<b>(10,823)</b>	<b>(4,687)</b>	<b>—</b>



# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(prepared in accordance with HKFRS)

## 21. DEFERRED INCOME TAX (Continued)

The movement in deferred income tax assets and liabilities during the year is as follows:

### Deferred income tax assets

#### Group

	Provisions for assets		Provision for employee benefits		Others		Total	
	2006 RMB'000	2005 RMB'000	2006 RMB'000	2005 RMB'000	2006 RMB'000	2005 RMB'000	2006 RMB'000	2005 RMB'000
At 1 January	(20,237)	(23,042)	(17,673)	(20,210)	(15,435)	(5,903)	(53,345)	(49,155)
Charged / (credited) to income statement	4,257	2,805	1,475	2,537	(17,339)	(9,532)	(11,607)	(4,190)
At 31 December	(15,980)	(20,237)	(16,198)	(17,673)	(32,774)	(15,435)	(64,952)	(53,345)

#### Company

	Provisions for assets		Provision for employee benefits		Others		Total	
	2006 RMB'000	2005 RMB'000	2006 RMB'000	2005 RMB'000	2006 RMB'000	2005 RMB'000	2006 RMB'000	2005 RMB'000
At 1 January	—	—	—	—	—	—	—	—
Charged / (credited) to income statement	(3,424)	—	(70)	—	(1,193)	—	(4,687)	—
At 31 December	(3,424)	—	(70)	—	(1,193)	—	(4,687)	—

### Deferred income tax liabilities - Group

	Property, plant, and equipment revaluation	
	2006 RMB'000	2005 RMB'000
At 1 January	42,522	43,174
Credited to income statement	(652)	(652)
At 31 December	41,870	42,522

## 22. EMPLOYEE BENEFITS — GROUP

	2006 RMB'000	2005 RMB'000
Medical insurance scheme	60,197	53,586
Housing allowance scheme	15,694	19,276
	75,891	72,862
Less: Current portion of employee benefits included in other payables and accrued charges	(25,753)	(26,659)
	50,138	46,203



# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(prepared in accordance with HKFRS)

## 23. OTHER INCOME — NET

	2006 RMB'000	2005 RMB'000
Gain on dilution of interest in a subsidiary	—	19,819
Interest income *	—	10,522
Gross rental income from investment properties	25,711	22,796
Gross rental income from other properties	11,032	16,758
Royalty income	2,866	2,579
Dividend income from available-for-sale financial assets	4,567	3,405
Income arising from disposals of financial assets at fair value through profit and loss	6,038	—
Others	24,982	15,715
	<u>75,196</u>	<u>91,594</u>

\* Interest income earned for the year ended 31 December 2006 has been included in finance costs — net.

## 24. EXPENSES BY NATURE

Cost of goods sold, selling and marketing costs and administrative expenses are analysed as below:

	2006 RMB'000	2005 RMB'000
Depreciation and amortisation (Notes 6, 8 and 9)	145,428	142,556
Impairment charge of available-for-sale financial assets (Note 13)	1,769	2,093
Impairment charge of goodwill	—	2,004
Impairment charge of property, plant, and equipment (Note 6)	209	—
Decline in value of financial assets at fair value through profit or loss	1,951	7,659
Impairment charge of receivables, net of reversal	10,801	5,740
Net impairment charge / (reversal of impairment charge) of inventories (Note 14)	2,627	(2,794)
Outgoings in respect of investment properties	3,809	3,713
Loss on disposal of property, plant, and equipment (Note 31)	2,516	4,072
Research and development expenses	36,926	37,984
Transportation	59,397	63,034
Advertising costs	206,110	196,136
Changes in finished goods and work in progress (Note 14)	(23,235)	(26,932)
Raw materials and consumables used	1,248,465	999,310
Changes in merchandise (Note 14)	(109,095)	(45,863)
Merchandise purchased	7,221,571	6,404,489
Auditors' remuneration	3,488	3,300
Operating leases for buildings	33,034	33,377
Employee benefit expenses (Note 25)	680,823	631,690
Other expenses	380,328	269,592
	<u>9,906,922</u>	<u>8,731,160</u>





# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(prepared in accordance with HKFRS)

## 25. EMPLOYEE BENEFIT EXPENSES

(a) Employee benefit expenses are analysed as follows:

	2006 RMB'000	2005 RMB'000
Pension benefit	68,145	64,584
Housing fund	42,637	41,855
Medical insurance	36,864	34,054
Housing allowances	13,090	19,005
Salaries, wages and other staff benefits	520,087	472,192
	<u>680,823</u>	<u>631,690</u>
Number of employees	<u>8,223</u>	<u>8,600</u>

(b) Directors' and supervisors' emoluments

The remuneration of every director and supervisor for the year ended 31 December 2006 is set out below:

	Fees RMB'000	Salaries and other benefits RMB'000	Bonuses RMB'000	Retirement scheme contributions RMB'000	Total RMB'000
<b>Name of director</b>					
Yang Rongming (a)	—	207	100	—	307
Zhou Yuejin (b)	—	73	159	—	232
Xie Bin (c)	—	96	281	—	377
Chen Zhinong (a and d)	—	92	93	—	185
Feng Zansheng (e)	—	130	481	—	611
Wu Zhang	80	—	—	—	80
Wong Hin Wing	80	—	—	—	80
Zhang Heyong	80	—	—	—	80
<b>Name of supervisor</b>					
Chen Canying (a)	—	190	58	—	248
Ouyang Qiang	—	111	45	—	156
Zhong Yugan	—	30	—	—	30



# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(prepared in accordance with HKFRS)

## 25. EMPLOYEE BENEFIT EXPENSES (Continued)

### (b) Directors' and supervisors' emoluments (continued)

The remuneration of every director and supervisor for the year ended 31 December 2005 is set out below:

Name of director	Fees RMB'000	Salaries and other benefits RMB'000	Bonuses RMB'000	Retirement scheme contributions RMB'000	Total RMB'000
Yang Rongming (a)	—	311	96	—	407
Zhou Yuejin(b)	—	147	160	18	325
Xie Bin (c)	—	179	—	18	197
Feng Zansheng (e)	—	140	1,045	18	1,203
Wu Zhang	80	—	—	—	80
Wong Hin Wing	80	—	—	—	80
Zhang Heyong	80	—	—	—	80
He Shuhua (f)	—	46	40	6	92
<b>Name of supervisor</b>					
Chen Canying (a)	—	127	60	—	187
Ouyang Qiang	—	141	—	18	159
Zhong Yugan	—	30	—	—	30

Notes:

- (a) The director or supervisor received emoluments from the parent company, part of which is in respect of his services to the Company and its subsidiaries. No apportionment has been made as the director considers that it is impracticable to apportion this amount between their services to the Group and their services to the Company's parent company.
- (b) Resigned on 27 April 2006.
- (c) Resigned on 15 June 2006.
- (d) Appointed on 15 June 2006.
- (e) The director received emoluments from the subsidiaries in respect of his services to the Company and its subsidiaries.
- (f) Resigned on 27 April 2005.

No directors and supervisors waived or agreed to waive any emoluments in respect of the year ended 31 December 2006 and 31 December 2005.



# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(prepared in accordance with HKFRS)

## 25. EMPLOYEE BENEFIT EXPENSES (Continued)

### (c) Five highest paid individuals

The five individuals whose emoluments were the highest in the Group for the year include two (2005: three) directors whose emoluments are reflected in the analysis presented above. The emoluments payable to the remaining three (2005: two) individuals during the year are as follows:

	2006 RMB'000	2005 RMB'000
Basic salaries and allowances	374	283
Bonuses	1,327	905
Retirement scheme contributions	—	36
	<u>          </u>	<u>          </u>

The emoluments fell within the following bands:

	Number of individuals	
	2006	2005
Emolument bands		
Nil - RMB1,000,000	<u>          3</u>	<u>          2</u>

## 26. FINANCE COSTS — NET

	2006 RMB'000	2005 RMB'000
Interest expense on borrowings	46,510	51,338
Other incidental borrowing costs	8,603	2,272
	<u>          </u>	<u>          </u>
Finance costs	55,113	53,610
Finance income — Interest income *	(9,753)	—
	<u>          </u>	<u>          </u>
Finance costs — net	<u>45,360</u>	<u>53,610</u>

\* Interest income earned for the year ended 31 December 2005 had been included in other income — net.



# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(prepared in accordance with HKFRS)

## 27. INCOME TAX EXPENSE

The PRC enterprise income tax has been provided at the principal rate of 33% (2005: 33%) on the estimated assessable profit for the year, except for a subsidiary and a jointly controlled entity which are foreign investment production enterprises and a subsidiary which is qualified as "Advanced Technology Enterprise". Given the subsidiary and the jointly controlled entity which are foreign investment production enterprise were established in a coastal economic development zone, the applicable enterprise income tax rate is 24%. The jointly controlled entity is entitled to an exemption from the PRC enterprise income tax for two years commencing from the first profit-making year and a 50% reduction in the enterprise income tax rate in the following three years. The applicable enterprise income tax rate for the subsidiary qualified as "Advanced Technology Enterprise" is 15%.

	2006 RMB'000	2005 RMB'000
Current income tax		
— PRC enterprise income tax	130,826	112,613
Deferred income tax (Note 21)	(12,259)	(4,842)
	<u>118,567</u>	<u>107,771</u>

The taxation on the Group's profit before income tax differs from the theoretical amount that would arise using the principal rate of the PRC enterprise income tax as follows:

	2006 RMB'000	2005 RMB'000
Profit before income tax	349,155	315,493
Calculated at a rate of 33% (2005: 33%)	115,221	104,112
Effect of different rates applicable to subsidiaries and a jointly controlled entity	(15,289)	(9,736)
Income not subject to taxation	(1,850)	(6,540)
Expenses not deductible for taxation purposes	20,485	19,935
Taxation charge	<u>118,567</u>	<u>107,771</u>

## 28. PROFIT ATTRIBUTABLE TO EQUITY HOLDERS OF THE COMPANY

The profit attributable to equity holders of the Company is dealt with in the financial statements of the Company to the extent of RMB183,259,000 (2005: RMB112,180,000).

## 29. EARNINGS PER SHARE

The calculation of earnings per share for the year ended 31 December 2006 is based on the profit attributable to equity holders of the Company of RMB218,067,000 (2005: RMB197,804,000) and the 810,900,000 (2005: 810,900,000) shares in issue.

No diluted earnings per share is presented as there were no potential dilutive shares in issue during the years ended 31 December 2006 and 2005.



# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(prepared in accordance with HKFRS)

## 30. DIVIDEND

	2006 RMB'000	2005 RMB'000
Final, proposed, of RMB0.084 (2005: RMB0.070) per share	<u>68,116</u>	<u>56,763</u>

At a meeting held on 27 April 2007, the directors declared a final dividend of RMB0.084 per share. The proposed dividend is not reflected as a dividend payable in these financial statements, but will be reflected as an appropriation of retained earnings for the year ending 31 December 2007.

The amount of profits available for the distribution to equity holders of the Company is the lower of the amount determined in accordance with PRC accounting standards and systems and the amount determined in accordance with HKFRS.

## 31. NOTES TO THE CONSOLIDATED CASH FLOW STATEMENT

### (a) Cash generated from operations

	2006 RMB'000	2005 RMB'000
Profit for the year	230,588	207,722
Adjustments for:		
— Taxation (Note 27)	118,567	107,771
— Depreciation (Note 6)	126,633	125,389
— Amortisation (Note 8 & 9)	18,795	17,167
— Impairment expense (Note 24)	17,357	14,702
— loss on disposal of property, plant and equipment *	2,516	4,072
— Interest income (Note 26)	(9,753)	(10,522)
— Profit arising from dilution of equity interest in a subsidiary	—	(19,819)
— Dividend income arising from available for-sale financial assets (Note 23)	(4,567)	(3,405)
— Income arising from disposal of financial assets at fair value through profit and loss (Note 23)	(6,038)	—
— Finance costs (Note 26)	46,510	51,338
— Share of losses from associates (Note 11)	279	1,212
	<u>540,887</u>	495,627
Changes in working capital:		
— Inventories	(180,502)	(85,687)
— Trade and other receivables	(339,074)	(155,838)
— Trade and other payables	119,250	(15,216)
Cash generated from operations	<u>140,561</u>	<u>238,886</u>



# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(prepared in accordance with HKFRS)

## 31. NOTES TO THE CONSOLIDATED CASH FLOW STATEMENT (Continued)

### (a) Cash generated from operations (continued)

\* In the cash flow statement, proceeds from sale of property, plant and equipment comprise:

	2006 RMB'000	2005 RMB'000
Net book amount (Note 6)	8,226	5,302
Loss on disposal of property, plant and equipment (Note 24)	<u>(2,516)</u>	<u>(4,072)</u>
Proceeds from disposal of property, plant and equipment	<u><u>5,710</u></u>	<u><u>1,230</u></u>

### (b) Disposal of a subsidiary

Information relating to disposal of a subsidiary on 30 April 2006 is as below:

	RMB'000
Total assets	2,389
Total liabilities	<u>(22)</u>
Net assets	<u><u>2,367</u></u>
Net assets received by the Group	1,565
Net assets received by minority shareholder	<u>802</u>
Net assets of a subsidiary disposed of	<u><u>2,367</u></u>
The net cash flow on disposal of the subsidiary is as follows:	
Proceeds received from the disposal	798
Less: cash and bank balances in the subsidiary disposed of	<u>(1,600)</u>
Proceeds received from the disposal, net of cash held by the subsidiary	<u><u>(802)</u></u>

There were no disposals of subsidiaries during the year ended 31 December 2005 and accordingly, no comparative information is presented.



# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(prepared in accordance with HKFRS)

## 32. COMMITMENTS

### (a) Capital Commitments

Capital expenditure at the balance sheet date but not yet incurred is as follows:

	Group	
	2006 RMB'000	2005 RMB'000
Property, plant and equipment Contracted but not provided for	12,677	23,412
Authorised but not contracted for	13,580	38,036
	<u>26,257</u>	<u>61,448</u>

### (b) Commitments under operating leases

At 31 December 2006, the future aggregate minimum lease rental receivables under non-cancellable operating leases in respect of buildings are as follows:

	Group		Company	
	2006 RMB'000	2005 RMB'000	2006 RMB'000	2005 RMB'000
Not later than 1 year	26,610	20,315	721	1,093
Later than 1 year and not after than 5 years	42,260	44,705	—	721
Later than 5 years	21,868	19,908	—	—
	<u>90,738</u>	<u>84,928</u>	<u>721</u>	<u>1,814</u>

### (c) Future operating lease receivables

At 31 December 2006, the future aggregate minimum lease receivables under non-cancellable operating leases in respect of building are as follows:

	Group	
	2006 RMB'000	2005 RMB'000
Not later than 1 year	31,949	23,389
Later than 1 year and not later than 5 years	35,487	47,047
Later than 5 years	4,911	—
	<u>72,347</u>	<u>70,436</u>



# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(prepared in accordance with HKFRS)

## 33. RELATED-PARTY TRANSACTIONS

The directors regard Guangzhou Pharmaceutical Holdings Limited ("GZPHL"), a PRC state-owned enterprise under the control and supervision of the Guangzhou Municipal Government, being the ultimate holding company.

Save as disclosed elsewhere in the consolidated financial statements, significant related party transactions, which were carried out in the normal course of the Group's business are as follows:

	Note	2006 RMB'000	2005 RMB'000
<b>Ultimate holding company</b>			
License fee expenses	a	10,782	12,230
Service fee expenses	b	939	860
Welfare facilities fee expenses	c	274	310
Rental expenses	d	2,944	3,450
		<u>14,939</u>	<u>16,850</u>
<b>A jointly controlled entity</b>			
Sales of raw materials	e	40,194	20,700
Purchase of finished goods	e	96,605	26,310
		<u>136,799</u>	<u>47,010</u>
<b>Associates</b>			
Advertising expenses	e	19,144	—
<b>Fellow subsidiaries</b>			
Sales of finished goods and raw materials	e	196,786	201,295
Purchases of finished goods and raw materials	e	555,962	456,860
		<u>752,748</u>	<u>658,155</u>
<b>Other state-controlled entities</b>			
Sales of finished goods and raw materials	e	3,331,272	2,170,470
Purchases of finished goods and raw materials	e	1,175,509	768,546
Purchases of machinery and equipment	e	1,729	7,342
Service fee expenses	g	85,230	76,792
		<u>4,593,740</u>	<u>3,023,150</u>
		<b>2006 RMB'000</b>	<b>2005 RMB'000</b>
<b>Key management compensation</b>			
Salaries and other benefits		1,212	1,269
Bonuses		2,004	1,327
Retirement scheme contributions		—	107
		<u>3,216</u>	<u>2,703</u>





# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(prepared in accordance with HKFRS)

## 33. RELATED-PARTY TRANSACTIONS (Continued)

### Year-end balances arising from sales/purchases of goods/services

	Note	2006 RMB'000	2005 RMB'000
Due from ultimate holding company		<u>4,071</u>	<u>5,060</u>
Due to ultimate holding company	i	<u>16,994</u>	<u>25,468</u>
Due from fellow subsidiaries	h	<u>82,236</u>	51,614
Less: Provision for impairment of receivables	h	<u>—</u>	(1,682)
		<u>82,236</u>	<u>49,932</u>
Due to fellow subsidiaries	i	<u>41,902</u>	<u>62,870</u>
Due from other state-controlled entities	h	<u>242,848</u>	368,524
Less: Provision for impairment of receivables	h	<u>(7,857)</u>	(10,580)
		<u>234,991</u>	<u>357,944</u>
Due to other state-controlled entities	i	<u>79,625</u>	<u>54,918</u>

Note:

- (a) Pursuant to the Trademark License Agreement entered into by the Company and GZPHL, its ultimate holding company, on 1 September 1997 and its supplementary agreement dated 28 July 2005, GZPHL has granted the Company, its subsidiaries and a jointly controlled entity, an exclusive right to use 38 trademarks owned by GZPHL for a term of 10 years. The Company agreed to pay a license fee for the use of the trademarks at 0.1% of the aggregate net sales of the Company and its subsidiaries and at 2.1% of the aggregate net sales of a jointly controlled entity.
- (b) Pursuant to the Accommodation Services Agreement entered into by the Company and GZPHL on 1 September 1997 and a supplemented notice dated 31 December 1997, GZPHL has agreed to continue to provide staff quarters to the employees of the Group. The Company agreed to pay a service fee equal to 6% per annum on the net book value of the relevant staff quarters. The Accommodation Services Agreement will expire on 31 December 2007.
- (c) Pursuant to the Composite Services Agreement entered into by the Company and GZPHL on 1 September 1997, GZPHL agreed to provide certain welfare facilities to the Group. The Group agreed to be responsible for the operation, management and maintenance of the facilities and pay a welfare facilities fee equal to GZPHL's total depreciation charges of the welfare facilities for the year ended 31 December 1997 plus a 10% annual increment based on the welfare facilities for the previous year. The Composite Services Agreement will expire on 31 December 2007.
- (d) Pursuant to the Tenancy Agreement and the Office Tenancy Agreement both entered into by the Company and GZPHL on 6 February 2004, GZPHL has granted to the Group the right to use certain premises such as warehouses and offices for a term of three and a half years at a fixed annual rent which is subject to the adjustment of standard rent as prescribed from time to time by Guangzhou Real Estate Administration Bureau, plus utilities and other outgoings which are payable based on actual consumption. The agreement will expire on 31 August 2007.
- (e) The sales and purchase transactions with the jointly controlled entity, associates, fellow subsidiaries and other state-owned entities were at terms similar to those transactions with other third parties.



# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(prepared in accordance with HKFRS)

## 33. RELATED-PARTY TRANSACTIONS (Continued)

Note: (continued)

- (f) GZPHL, the ultimate holding company, is a state-controlled entity directly controlled by the PRC government. The PRC government is the Company's ultimate controlling party. State-controlled enterprises and their subsidiaries, in addition to GZPHL group companies, directly or indirectly controlled by the PRC government are also related parties of the Group. Neither GZPHL nor the PRC government publishes financial statements available for public use.

The Group sells its products on wholesale and retail basis. The retail sales are conducted through the Group's retail outlets at market prices on cash basis. Due to the pervasiveness of the Group's retail transactions with the state-controlled enterprises' employees, the key management personnel and their close family members of state-controlled enterprises, and other related parties, there is no feasible way or a reliable system to track such transactions and ensure the completeness of the disclosure. Therefore, the sales of goods disclosed above do not include retail sales to related parties. Management believes that meaningful information relative to related party transaction has been adequately disclosed.

In addition, normal transactions entered into with financial institutions, public utilities providers and governmental departments and agencies have been excluded.

- (g) Service fees charged by other state-controlled enterprises are mainly in relation to advertising and promotion activities, commercial insurance and transportation. These transactions were entered into at open market terms.
- (h) The receivables from related parties arise mainly from sale transactions. The receivables are unsecured in nature and bear no interest.
- (i) The payables to related parties arise mainly from purchase transactions. The payables bear no interest.

## 34. PRINCIPAL SUBSIDIARIES

The following is a list of the principal subsidiaries as at 31 December 2006:

Name	% of equity interest held		Registered capital RMB	Principal activities
	Directly	Indirectly		
Guangzhou First Chinese Medicine Company Limited <sup>3</sup>	100.00	—	166,000,000	Production of CPM
Guangzhou Chen Li Ji Chinese Medicine Factory <sup>1</sup>	100.00	—	94,000,000	Production of CPM
Guangzhou Qi Xing Pharmaceutical Factory <sup>1</sup>	100.00	—	82,416,741	Investment Holdings
Guangzhou Jing Xiu Tang Pharmaceutical Co., Ltd. <sup>3</sup>	88.40	—	86,232,345	Production of CPM
Guangzhou Pan Gao Shou Pharmaceutical Co., Ltd. <sup>3</sup>	87.77	—	65,436,232	Production of CPM
Guangzhou Xing Qun Pharmaceutical Co., Ltd. <sup>3</sup>	88.99	—	77,168,904	Production of CPM
Guangzhou Pharmaceutical Corporation Limited <sup>2</sup>	90.09	6.90	222,000,000	Trading of western pharmaceutical products and medical apparatus
Guangzhou Chinese Medicine Corporation <sup>1</sup>	100.00	—	72,026,905	Trading of CPM and Chinese raw medicine
Guangzhou Pharmaceutical Corporation Jianmin Medicine Chain Pharmacies <sup>1</sup>	—	96.99	10,694,000	Wholesale and retailing of medicine, pharmaceutical and related products



# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(prepared in accordance with HKFRS)

## 34 PRINCIPAL SUBSIDIARIES (Continued)

Name	% of equity interest held		Registered capital RMB	Principal activities
	Directly	Indirectly		
Guangzhou Guo Xin Te Pharmaceutical Miscellaneous Medicine Wholesale Company <sup>1</sup>	—	96.99	3,000,000	Wholesale of miscellaneous medicine
Guangzhou Jiamin Medicine Pharmaceutical Sales and Marketing Company <sup>1</sup>	—	96.99	500,000	Wholesale of western pharmaceutical products
Guangzhou Pharmaceutical Import & Export Corporation <sup>1</sup>	100.00	—	2,568,000	Import and export of medicine
Guangzhou Qi Xing Pharmaceutical Co., Ltd. <sup>4</sup>	—	75.00	100,000,000	Production of CPM
Guangzhou Chinese Medicine Corporation Chinese Medical Drink and Pill Factory <sup>1</sup>	—	100.00	3,113,000	Processing of health care beverages and drinks
Guangzhou Chinese Medicine Corporation Medical Powder and Herb Wholesale Company <sup>1</sup>	—	100.00	534,000	Wholesale of Chinese raw medicine
Guangzhou Chinese Medicine Corporation Sales and Marketing Company <sup>1</sup>	—	100.00	2,083,000	Wholesale and retailing of CPM
Guangzhou Chinese Medicine Corporation Cai Zhi Lin Medicine Chain Pharmacies <sup>1</sup>	—	100.00	3,934,000	Retailing of Chinese raw medicine and CPM
Guangzhou Medical Equipment and Chemical Testing Equipment Co., Ltd. <sup>2</sup>	—	89.32	11,880,000	Wholesale and retailing of medical apparatus and chemical testing equipment
Guangzhou Hanfang Contemporary Chinese Medicine Research and Development Co., Ltd. <sup>2</sup>	70.04	2.91	127,764,300	Research and development of CPM
Guangzhou Baidi Biological Pharmaceutical Co., Ltd. <sup>2</sup>	95.69	—	83,600,000	Research and development of patented biological products
Guangzhou Huanye Medicine Co., Ltd. <sup>2</sup>	100.00	—	6,000,000	Production of western pharmaceutical products
Guangzhou Guo Ying New and Special Medicine Wholesale Company <sup>1</sup>	—	96.99	9,070,000	Wholesale of medicine and health care products
Guangzhou Pharmaceutical Group Yingbang Marketing Co., Ltd. <sup>2</sup>	51.00	—	18,407,863	Wholesale of medicine and health care products
Guangxi Ying Kang Pharmaceutical Co., Ltd. <sup>2</sup>	51.00	—	31,884,529	Production of CPM



# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(prepared in accordance with HKFRS)

## 34 PRINCIPAL SUBSIDIARIES (Continued)

Except for the change in equity interest in Guangzhou First Chinese Medicine Company Limited from 97.02% to 100% and Guangzhou Huanye Medicine Co., Ltd from 59.70% to 100% during the year, there has not been any change in equity interest in other principal subsidiaries held by the Group since 31 December 2005.

The above principal subsidiaries are all operated in the PRC.

Kind of legal entities:

- <sup>1</sup> State-owned enterprise
- <sup>2</sup> Limited company
- <sup>3</sup> Joint stock company
- <sup>4</sup> Sino-foreign joint venture

## 35 EVENTS AFTER BALANCE SHEET DATE

- (a) On 16 March 2007, the National People's Congress approved the Corporate Income Tax Law of the PRC (the "new CIT Law"), which is effective from 1 January 2008. Under the new CIT Law, group companies which currently adopt corporate income tax at the rate of 33% will be subject to the rate of 25% from 1 January 2008.

Since the deferred tax assets and deferred tax liabilities shall be measured at the tax rates that are expected to apply to the period when the asset is realised or the liability is settled, the change in the applicable tax rate will affect the determination of the carrying values of deferred tax assets and deferred tax liabilities of the Group. As at the date that these financial statements are approved for issue, detailed measures of the new CIT Law have yet to be issued. Subject to detailed measures and other related regulations concerning computation of taxable income, as well as specific preferential tax treatments and their related transitional provisions, the Group has performed a preliminary assessment on the balances of the deferred tax assets and liabilities as at 31 December 2006 and estimated that the deferred tax assets would be written down by approximately RMB11,132,000 and the deferred tax liabilities would be written down by approximately RMB10,150,000 as the result of the change in the applicable tax rate. The Group will further evaluate the impact on its operating results and financial positions of future periods as more detailed measures and other related regulations are announced.

- (b) Guangzhou Pharmaceutical Corporation Limited ("GPC Limited") is a principal subsidiary of the Company. On 27 January 2007, all other investors of GPC Limited, except for the Company have entered into "a share transfer agreement" with Alliance BMP, whereby the other investors agreed to transfer all their respective equity interests in GPC Limited to Alliance BMP.

In addition, on 27 January 2007, the Company has entered into an agreement with Alliance BMP, whereby both parties agreed to increase the registered capital of GPC Limited from RMB222,000,000 to RMB400,000,000. Upon completion of the above transactions, the Company and Alliance BMP each owns 50% equity interest in GPC Limited. Since then, GPC Limited will cease to be a subsidiary of the Company and will become a jointly controlled entity of the Company.



## Documents Available for Inspection

- (i) The original copy of the annual report signed by the Chairman of the Board of the Company;
- (ii) The financial statements signed by the legal representative and the Financial Controller of the Company;
- (iii) The auditor's reports sealed and signed by Guangdong Yangcheng Certified Public Accountants Co., Ltd. and PricewaterhouseCoopers, together with the financial statements prepared by them in accordance with PRC Accounting Standards and Systems and HKFRS, respectively;
- (iv) The original company documents disclosed and announcements published in Shanghai Securities, Hong Kong Economic Times and The Standard during the Reporting Period;
- (v) The documents listed above are available at the Secretariat to the Board, located at 2nd Floor, 45 Sha Mian North Street, Guangzhou, Guangdong, the PRC.

