INTRODUCTION

The Company was incorporated on 17th December, 2001 as an investment holding company pursuant to the Reorganisation. The business activities of the Group are primarily carried out through Zhaoke, a sino-foreign equity joint venture established in the PRC and which is owned as to 70 per cent. by the Group and as to 30 per cent. by USTC Biotech. Located in Hefei, Anhui Province, the PRC, Zhaoke is an integrated research-driven and market-oriented pharmaceutical company engaged in the development, manufacture and sales of quality biopharmaceutical products that focus on combating cardiovascular diseases and viral sexually transmitted diseases. Since its establishment in 1994, Zhaoke has developed three technology platforms, namely, (i) the snake venom technology, (ii) the low molecular weight heparin technology, and (iii) the water-based gel delivery system. As at the Latest Practicable Date, the Group manufactures and sells three self-developed biopharmaceutical products for the medical treatment of stroke, cardiovascular diseases and viral sexually transmitted diseases such as genital warts, respectively, details of which are set out in the paragraph headed "Products" in this section. In addition, the Group has (i) three other products, the application for clinical trials of which have been submitted and the relevant clinical trials are anticipated to be commenced in 2002 and 2003, and (ii) five products identified for research and development with a view to commercialisation. The Group carries out its sales and distribution activities through Zhaoke's sales offices located in Guangzhou and Hefei, the PRC and through appointing independent distributors in the PRC. The sales offices of Zhaoke, together with its branch offices in Beijing and Shanghai, are responsible for marketing and after-sales services in a designated region arranged in advance by the chief marketing officer of the Group. The Group's products are all sold in the PRC under the brandname of "ZHAOKE".

Zhaoke has two fully operational and GMP — compliant workshops for the production of (i) bulk pharmaceutical for injection and lyophilized powder for injection, and (ii) gel. Since its establishment in 1994, Zhaoke has received various awards in the PRC for its achievements in research and development works in the pharmaceutical industry, details of which are set out in the paragraph headed "Awards" in this section.

With the support of an experienced, dynamic and professional management team, the Group is able to respond quickly to customers' needs and to meet the challenges of the biopharmaceutical industry both in the PRC and overseas. Moreover, the Group has a scientific advisory board, which comprises mainly leading researchers from universities and research institutes in Hong Kong and the PRC, thus enabling the Group to have better access to the latest technological development in the biopharmaceutical field. Furthermore, the Group's research and development team has close working relationship with universities and research institutions in the PRC and Hong Kong (such as 中國藥科大學 (China Pharmaceutical University), 中國藥品生物製品檢定所 (China Drug Evaluation Institute) and the Biological Research Institute of the Hong Kong University of Science and Technology) which provides a strong foundation for future development of the Group's new products. The Group will also work to expand its research and development base by establishing partnership with Zengen, a biotechnology company based in the United States. The Group will continue to focus its efforts on drug researches and innovation, based on its three in-house developed technology platforms, to further develop its new products in the pipeline.

The Directors believe that with a strong research and development team, two modernised GMP-compliant biopharmaceutical workshops, three in-house developed technology platforms, a pipeline of new products and an effective and efficient management team, the Group is in a position to capitalise and leverage on the high standard of medical and scientific research and development that blend advanced technology with practical applications of the Group. The Group will focus its efforts on the patients' needs and deliver innovative and quality pharmaceutical products of value that combat diseases and improve health.

HISTORY AND DEVELOPMENT

Zhaoke was established on 7th February, 1994 as a sino-foreign equity joint venture and is owned as to 70 per cent. by Lee's Pharmaceutical and 30 per cent. by USTC Biotech for a period of twenty years expiring on 6th February, 2014. Both the total amount of investment and the registered capital of Zhaoke are US$2 million (equivalent to approximately HK$15.6 million). The respective share of the registered capital of Zhaoke had been paid up by Lee's Pharmaceutical as to US$1,400,000 (equivalent to approximately HK$10,920,000) in the form of cash and by USTC Biotech as to US$600,000 (equivalent to approximately HK$4,680,000) in the form of technology of protein extraction and purification from snake venom with enzymatic activities.

Lee's Pharmaceutical is the foreign party to Zhaoke and was established on 28th December, 1993. After Dr. Li Xiao Yi had completed his postdoctoral fellowship with Warner-Lambert (being a major pharmaceutical company in the United States), he decided to team up with his family member (namely, Mr. Lee Siu Fung, Siegfried) and his colleague (namely, Mr. Lee Sheung Yam) to tap in the pharmaceutical industry via Lee's Pharmaceutical as the common vehicle. Lee's Pharmaceutical was then owned as to (i) 50 per cent. by Mr. Lee Siu Fung, Siegfried; (ii) 25 per cent. by Dr. Li Xiao Yi; and (iii) 25 per cent. by Mr. Lee Sheung Yam. In 1996, Mr. Lee Sheung Yam transferred his then entire shareholding interest in Lee's Pharmaceutical to Mr. Lee Siu Fung, Siegfried.

Since its establishment, Zhaoke had been focusing mainly on the research and development of pharmaceutical products in the PRC. In May 1997, with an aim to capture the business opportunity from commercialisation of the products developed by Zhaoke, Ms. Lee and Ms. Leelalertsuphakun injected new funding into Lee's Pharmaceutical and became the new controlling shareholders of Lee's Pharmaceutical in lieu of Mr. Lee Siu Fung, Siegfried. Since then, Ms. Lee has been in charge of the financial matters of the Group and Ms. Leelalertsuphakun has been in charge of the operation and marketing affairs of the Group. In October 1997, the Group managed to launch its first product (namely, Defibrase) as approved by MOH (as a category 4 biopharmaceutical product) and take a big step forward by transforming itself from a pharmaceutical research company into an established pharmaceutical manufacturer.

In December 1997 and March 1998, Mr. Lee Siu Fung, Siegfried disposed of his then entire shareholding interest in Lee's Pharmaceutical to (i) Dr. Li Xiao Yi (representing 12.5 per cent. of the then total share capital of Lee's Pharmaceutical) and (ii) Triumph Leader (which is a company wholly owned by the spouse of Mr. Lee Siu Fung, Siegfried) (representing 25 per cent. of the then total share capital of Lee's Pharmaceutical). In March 1998, High Knowledge (which is a company wholly owned by Ms. Lue engaging in investments of pharmaceutical technologies) acquired from her spouse, Dr. Li Xiao Yi, the then entire shareholding interest

in Lee's Pharmaceutical (representing 25 per cent. of the then total share capital of Lee's Pharmaceutical). In June 2000, in view of the proven products launch and market development of the Group, Ms. Lee and Ms. Leelalertsuphakun further strengthen their controlling shareholding position in Lee's Pharmaceutical by acquiring from Triumph Leader for further equity interests in Lee's Pharmaceutical and increased their shareholding in Lee's Pharmaceutical from 50 per cent. to 75 per cent.

The key shareholding change of Lee's Pharmaceutical is summarised in the following table:

	1994 *(Notes A, B and C)*	**1996** *(Note D)*	**1997** *(Note E)*	**1997-1998** *(Notes F and G)*	**1998** *(Note H)*	**2000** *(Note I)*
1. Mr. Lee Siu Fung, Siegfried	50.0%	75.0%	37.5%	0.0%	0.0%	0.0%
2. Dr. Li Xiao Yi	25.0%	25.0%	12.5%	25.0%	0.0%	0.0%
3. Mr. Lee Sheung Yam	25.0%	0.0%	0.0%	0.0%	0.0%	0.0%
4. Ms. Lee and Ms. Leelalertsuphakun (or their common vehicle)	0.0%	0.0%	50.0%	50.0%	50.0%	75.0%
5. Triumph Leader	0.0%	0.0%	0.0%	25.0%	25.0%	0.0%
6. High Knowledge	0.0%	0.0%	0.0%	0.0%	25.0%	25.0%

**Notes:* Please refer to the transactions with the same numbering in the next table

In February 2002, with a view to enhancing its research and development potential and corporate profile, the Group brought in Zengen, a biotechnology company based in the United States, as a strategic investor who has contributed and transferred to the Group its peptide technology for the treatment of vaginitis for the benefit of the Company.

Whilst Zhaoke serves as the manufacturing arm of the Group, Lee's Pharmaceutical acts as the management arm of the Group and for collaborating with other institutes for research to license technology and products. Lee's China, owned as to 100 per cent. by Lee's Pharmaceutical, was incorporated on 20th October, 2000 with a view to provide marketing service to the Group's operation in the PRC. As at the Latest Practicable Date, Lee's China has not provided any marketing service to Zhaoke.

In preparation for the listing of the Shares on GEM, the Group underwent the Reorganisation whereby the Company became the ultimate holding company of the Group, particulars of which are set out under the paragraph headed "Corporate reorganisation" in Appendix IV to this prospectus. The following tables summarise the transfer and/or subscription of the equity interests of Lee's Pharmaceutical and capital contribution to Zhaoke (both being the key subsidiaries of the Company) since their respective incorporation dates.

Lee's Pharmaceutical (incorporated on 28th December, 1993)

Serial	Date of registration as shareholder	Name of shareholder	Name of vendor (if applicable)	Consideration	Number of shares	Percentage of equity interest (before the Placing)
	28/12/1993	the late Leelalertsupgul Preecha *(note 1)*	N/A	HK$1	1	N/A
	28/12/1993	Lelalertsuphakun Dusanee *(note 2)*	N/A	HK$1	1	N/A
	30/6/1994	Lee Siu Fung, Siegfried *(note 3)*	the late Leelalertsupgul Preecha	HK$1	1	N/A
	30/6/1994	Lee Siu Fung, Siegfried	Lelalertsuphakun Dusanee	HK$1	1	N/A
A	30/6/1994	Lee Siu Fung, Siegfried	N/A	HK$1,599,998	1,599,998	N/A
B	30/6/1994	Lee Sheung Yam *(note 4)*	N/A	HK$800,000	800,000	N/A
C	30/6/1994	Li Xiao Yi *(note 5)*	N/A	HK$800,000	800,000	N/A
D	13/2/1996	Lee Siu Fung, Siegfried	Lee Sheung Yam	HK$800,000	800,000	N/A
	13/2/1996	Philip Erdoes *(note 6)*	Li Xiao Yi	Gift (the instrument of transfer was stamped at HK$807)	384,000	N/A
E	1/5/1997	Lee's Machinery *(note 7)*	N/A	HK$3,200,000 (funded by internal resources of Lee's Machinery and not funded by Mr. Lee Siu Fung, Siegfried)	3,200,000	N/A
F	9/1/1998	Li Xiao Yi	Lee Siu Fung, Siegfried	HK$1 (the bought and sold notes was stamped at HK$939)	800,000	N/A
	9/1/1998	Li Xiao Yi	Philip Erdoes	Gift (the instrument of transfer was stamped at HK$903)	384,000	N/A
G	6/3/1998	Triumph Leader	Lee Siu Fung, Siegfried	HK$1 (the bought and sold notes was stamped at HK$1,876)	1,600,000	N/A
H	6/3/1998	High Knowledge *(note 8)*	Li Xiao Yi	HK$1 (the bought and sold notes was stamped at HK$1,876)	1,600,000	N/A
	5/4/2000	Huby Technology *(note 9)*	Lee's Machinery	HK$627,050	3,200,000	N/A

Serial	Date of registration as shareholder	Name of shareholder	Name of vendor (if applicable)	Consideration	Number of shares	Percentage of equity interest (before the Placing)
I	5/7/2000	Dynamic Achieve *(note 10)*	Triumph Leader	HK$313,525	1,600,000	N/A
	27/12/2001	Techfarm *(note 11)*	Dynamic Achieve	HK$800,000	800,000	N/A
	31/12/2001	Huby Technology	N/A	HK$12,000,000	12,000,000	N/A
	4/2/2002	Lee's International	Dynamic Achieve	HK$400,000 worth of shareholding interest in Lee's Pharmaceutical as a result of the share swap	800,000	4.35%
			High Knowledge	HK$800,000 worth of shareholding interest in Lee's Pharmaceutical as a result of the share swap	1,600,000	8.70%
			Huby Technology	HK$7,600,000 worth of shareholding interest in Lee's Pharmaceutical as a result of the share swap	15,200,000	82.60%
			Techfarm	HK$400,000 worth of shareholding interest in Lee's Pharmaceutical as a result of the share swap	800,000	4.35%
				Total	18,400,000	100.0%

Notes:

1. The late Mr. Leelalertsupgul Preecha is the father of Ms. Lee and Ms. Leelalertsuphakun. He was a director of Lee's Pharmaceutical during 9th February, 1994 to 15th April, 1994.

2. Triumph Leader is a limited liability company incorporated in Hong Kong whose entire issued share capital at the time of transfer was beneficially owned by Ms. Lelalertsuphakun Dusanee who is the spouse of Mr. Lee Siu Fung, Siegfried and the sister-in-law of each of Ms. Lee and Ms. Leelalertsuphakun. Ms. Lelalertsuphakun Dusanee was never a director of Lee's Pharmaceutical.

3. Mr. Lee Siu Fung, Siegfried is the brother of each of Ms. Lee and Ms. Leelalertsuphakun. Further Information on Mr. Lee Siu Fung, Siegfried is set out on the section headed "Relationship with past shareholders and directors of the Group".

4. Mr. Lee Sheung Yam is an independent third party not connected with any of the chief executive, directors, management shareholders, substantial shareholders or any of their respective associates. He was a director of Siu-Fung Ceramics Holdings Limited, a company listed on the Main Board and delisted in December 2001. He was a director of Lee's Pharmaceutical during period 15th April, 1994 to 23rd January, 1996.

5. Dr. Li Xiao Yi is the brother of each of Ms. Lee and Ms. Leelalertsuphakun. He was once a director of Siu-Fung Ceramics Holdings Limited, a company listed on the Main Board and delisted in December 2001. He was also a director of Lee's Pharmaceutical during 9th February, 1994 to 16th January, 2002.

6. Mr. Philip Erdoes is an independent third party not connected with any of the chief executive, directors, management shareholders, substantial shareholders or any of their respective associates. He was a director of Siu-Fung Ceramics Holdings Limited, a company listed on the Main Board and delisted in December 2001. He was never a director of Lee's Pharmaceutical.

7. Lee's Machinery is a limited liability company incorporated in Hong Kong which is owned as to 50 per cent. by Ms. Lee and 50 per cent. by Ms. Leelalertsuphakun.

8. High Knowledge is a company incorporated in BVI with limited liability, whose entire issued share capital is beneficially owned by Ms. Lue who is the sister-in-law of each of Ms. Lee and Ms. Leelalertsuphakun.

9. Huby Technology is a company incorporated in BVI with limited liability, whose entire issued share capital is owned as to 50 per cent. by Ms. Lee and 50 per cent. by Ms. Leelalertsuphakun.

10. Dynamic Achieve is a company incorporated in BVI with limited liability, whose entire issued share capital is owned as to 50 per cent. by Ms. Lee and 50 per cent. by Ms. Leelalertsuphakun.

11. Techfarm is a company incorporated in BVI with limited liability, whose entire share capital is beneficially owned by Ms. Yu Wa, an independent third party not connected with any of the chief executives, directors, management shareholders, substantial shareholders of the Company or their respective associates. Ms. Yu Wa is not a director of Lee's Pharmaceutical.

Zhaoke (established on 7th February, 1994)

Date of making full capital contribution	Name of party	Name of vendor (if applicable)	Consideration	Percentage of equity interest
2/9/1997	Lee's Pharmaceutical *(note 12)*	N/A	US$1,400,000	70.0%
29/11/1995	USTC Biotech	N/A	US$600,000 worth of intangible asset in form of a snake venom technology	30.0%
			Total	100.0%

Note:

12. Pursuant to a supplemental joint venture agreement dated 17th May, 1994, Lee's Pharmaceutical substituted Siu-Fung Ceramics Holdings Limited to become the foreign party to Zhaoke for no consideration.

RELATIONSHIP WITH PAST SHAREHOLDERS AND DIRECTORS OF THE GROUP

Relationship with Mr. Lee Siu Fung, Siegfried and his spouse

In (i) December 1997 and (ii) March 1998, Mr. Lee Siu Fung, Siegfried, being brother of Ms. Lee, Ms. Leelalertsuphakun and Dr. Li Xiao Yi, disposed of his (i) 12.5 per cent. and (ii) 25 per cent. of the then total share capital of shareholding interest in Lee's Pharmaceutical to (i) Dr. Li Xiao Yi and (ii) Triumph Leader (which was wholly owned by Ms. Lelalertsuphakun Dusanee) respectively and has since then ceased to be a shareholder in any member of the Group. On the other hand, Ms. Lelalertsuphakun Dusanee (being the spouse of Mr. Lee Siu Fung, Siegfried) and Triumph Leader were shareholders of Lee's Pharmaceutical during the period from 28th December, 1993 to 30th June, 1994 and during the period from 5th March, 1998 to 30th June, 2000 respectively. Mr. Lee Siu Fung, Siegfried was a director of Lee's Pharmaceutical during the period from 15th April, 1994 to 4th January, 2000. Mr. Lee Siu Fung, Siegfried has never been the director of Zhaoke and Ms. Lelalertsuphakun Dusanee has never been a director of any member of the Group.

Mr. Lee Siu Fung, Siegfried had been involved in statutory-related matters such as share allotment and change of name during the period when Mr. Lee Siu Fung, Siegfried was a director and shareholder of Lee's Pharmaceutical. Further, Mr. Lee Siu Fung, Siegfried had made a personal guarantee in favour of Lee's Pharmaceutical's bank borrowings, which had been fully repaid subsequent to the investment of Lee's Machinery in Lee's Pharmaceutical in May 1997. The bank signatories of the Group have not included Mr. Lee Siu Fung, Siegfried since 30th December, 1998. Ms. Lee and Ms. Leelalertsuphakun have full power to operate all bank accounts since November 1997. Ms. Lelalertsuphakun Dusanee has never had any cheque signing authority for the Group. During the Track Record Period, Ms. Lee and Ms. Leelalertsuphakun had been actively managing the business and daily operations of the Group and had spent a majority of time during the calendar years 2000 and 2001 to station in the Group's pharmaceutical plant in Hefei, the PRC.

As evidenced by the fact that the daily operation and the overall management of the Group have been totally and directly supervised by Ms. Lee and Ms. Leelalertsuphakun, Mr. Lee Siu Fung, Siegfried and Ms. Lelalertsuphakun Dusanee have not taken any role in the management of the Group since 4th January, 2000. The Directors confirmed that neither Mr. Lee Siu Fung, Siegfried nor Ms. Lelalertsuphakun Dusanee will have any future involvement in the management of the business and operation of the Group. Both Ms. Lee and Ms. Leelalertsuphakun have confirmed that they will continue to manage the Group after the listing of Shares on GEM with the same primary responsibility, and will not relinquish their active management role in the Group.

In May 2001, a bankruptcy order was made against Mr. Lee Siu Fung, Siegfried. In this regard, the Directors had sought for an independent counsel opinion as to the impact of the bankruptcy of Mr. Lee Siu Fung, Siegfried on the two aforesaid transactions. According to the counsel opinion, there is a fairly strong case to contend that the two aforesaid transactions are not subject to the anti-avoidance provisions introduced by the Bankruptcy (Amendments) Ordinance 1996 (which came into force since 1st April, 1998) but are subject to the old "fraudulent preference" provision of the Bankruptcy Ordinance (Chapter 6 of the Laws of Hong Kong) (which was effective prior to 1st April, 1998). In that case, the counsel is of the opinion

that since both transactions were entered into more than 6 months before the presentation of the bankruptcy petition against Mr. Lee Siu Fung, Siegfried in 2001, they are therefore not challengeable under the "fraudulence preference" provisions of the Bankruptcy Ordinance.

Mr. Lee Siu Fung, Siegfried and Dr. Li Xiao Yi were directors of Siu-Fung Ceramics Holdings Limited. Mr. Lee Siu Fung, Siegfried and Dr. Li Xiao Yi were publicly criticised by the Stock Exchange on 5th December, 2000 in respect of the failure to publish financial results of Siu-Fung Ceramics Holdings Limited within the required time frame. In addition, Mr. Lee Siu Fung, Siegfried and Ms. Lelalertsuphakun Dusanee had been under investigation and/or subject to hearings by the Insider Dealing Tribunal since February 2001.

Relationship with Siu-Fung Ceramics Holdings Limited

Pursuant to the Joint Venture Agreement, Siu-Fung Ceramics Holdings Limited was the foreign party to Zhaoke. The approval letter for the establishment of Zhaoke as a sino-foreign equity joint venture was issued by Hefei City Commission for Foreign Trade and Economic Cooperation on 5th February, 1994 with the foreign party being Siu-Fung Ceramics Holdings Limited. Pursuant to a supplemental joint venture agreement dated 17th May, 1994, Siu-Fung Ceramics Holdings Limited was substituted by Lee's Pharmaceutical as the foreign party to Zhaoke. Although no approval letter for the change to Lee's Pharmaceutical as the new foreign party to Zhaoke has ever been obtained from Hefei City Commission for Foreign Trade and Economic Cooperation, the PRC legal adviser to the Company is of the opinion that the aforesaid change of foreign party to Zhaoke was legal and proper under the PRC law on the basis that (i) a formal supplemental agreement was entered into between the parties in respect of such change; (ii) the board of directors of Zhaoke had duly approved the change; and (iii) the Certificate of Approval for the establishment of Zhaoke with Lee's Pharmaceutical being the new foreign party to Zhaoke was duly issued by the Anhui Provincial Government on 1st June, 1994. In addition, an explanatory note and an opinion were issued by Hefei City Commission for Foreign Trade and Economic Cooperation on 26th December, 2001 and 24th May, 2002, respectively and the explanatory note and the opinion clearly recognise that the change of foreign party to Zhaoke from Siu-Fung Ceramics Holdings Limited to Lee's Pharmaceutical took place on 1st June, 1994, the date when the Certificate of Approval referred to in (iii) above was issued.

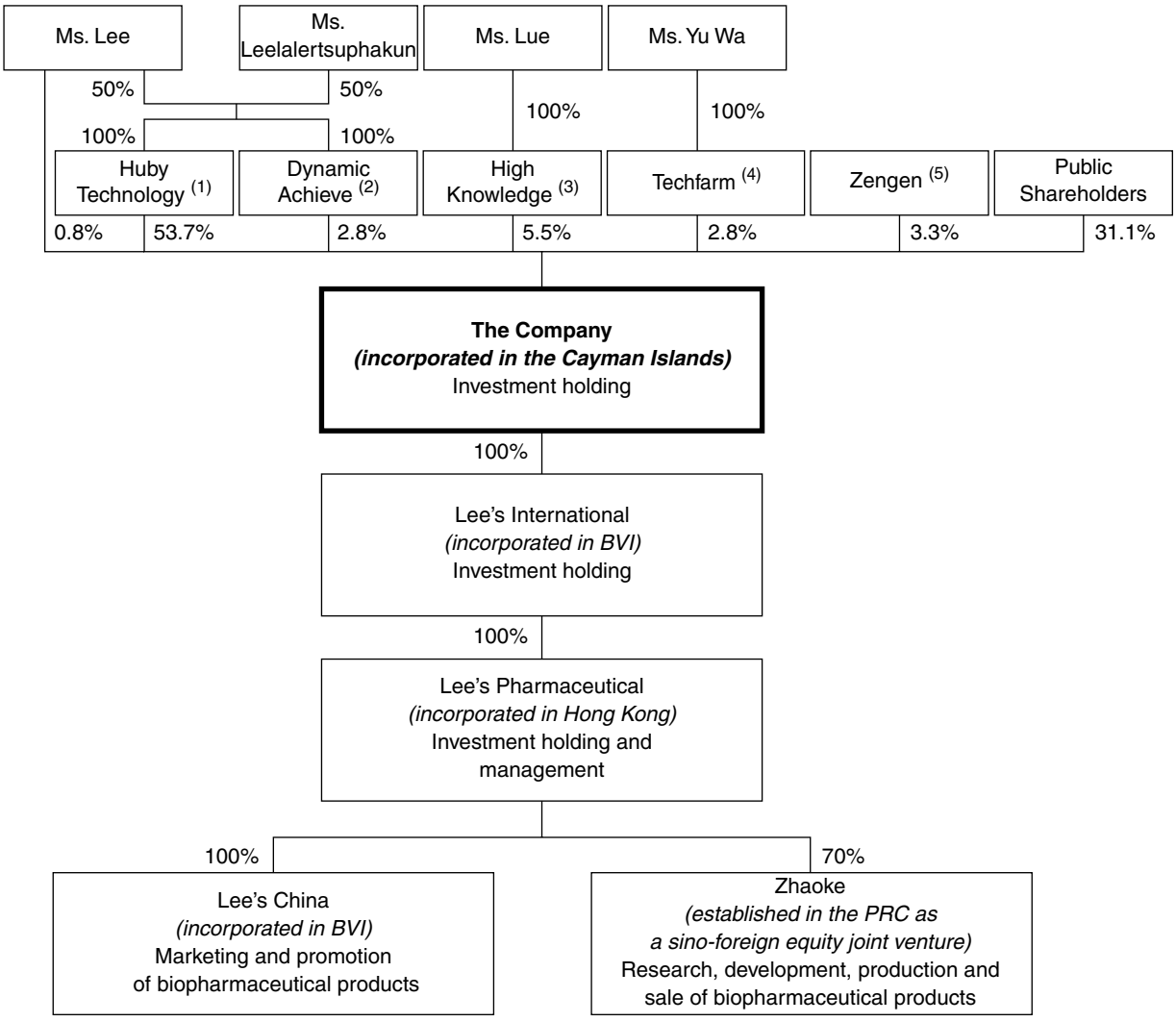
Siu-Fung Ceramics Holdings Limited was a company once listed on the Main Board but which was subsequently liquidated in May 2000 and delisted in December 2001. As set out in the section headed "Risk factors" in this prospectus, the liquidator of Siu-Fung Ceramics Holdings Limited may seek to void or challenge the change of foreign party to Zhaoke from Siu-Fung Ceramics Holdings Limited to Lee's Pharmaceutical. The Hong Kong legal adviser to the Company was of the view that, based on the fact that (i) Zhaoke is a validly and legally established enterprise; (ii) Siu-Fung Ceramics Holdings Limited had never made any capital contribution to Zhaoke; and (iii) the change took place approximately eight years ago and the change did not result in Siu-Fung Ceramics Holdings Limited becoming insolvent, there does not exist any solid basis for the liquidator of Siu-Fung Ceramics Holdings Limited to make any claim against the Group.

As set out in the section headed "History and development" in this prospectus, each of Mr. Lee Sheung Yam, Dr. Li Xiao Yi and Mr. Philip Erdoes was once a director of Siu-Fung Ceramics Holdings Limited. As elaborated in the same section in this prospectus, (i) Mr. Lee

Sheung Yam was (a) a shareholder and (b) a director of Lee's Pharmaceutical during the respective periods (a) from 30th June, 1994 to 13th February, 1996 and (b) from 15th April, 1994 to 23rd January, 1996; (ii) Dr. Li Xiao Yi was (a) a shareholder and (b) a director of Lee's Pharmaceutical during the respective periods (a) from 30th June, 1994 to 6th March, 1998 and (b) from 9th February, 1994 to 16th January, 2002; and (iii) Mr. Philip Erdoes was a shareholder of Lee's Pharmaceutical during the period from 13th February, 1996 to 9th January, 1998. In addition, the late Mr. To-Aramrut Chiewchan, being an elder brother of each of Mr. Lee Siu Fung, Siegfried, Ms. Leelalertsuphakun, Ms. Lee and Dr. Li Xiao Yi, was once a director of Siu-Fung Ceramics Holdings Limited. The late Mr. To-Aramrut Chiewchan was a director of Zhaoke during the period from 27th December, 1993 to 26th April, 1997.

CORPORATE STRUCTURE

The following chart showed the corporate structure of the Company, its Shareholders and its subsidiaries immediately after completion of the Placing (assuming the Over-allotment Option is not exercised):



Notes:

1. Huby Technology is a company incorporated in BVI with limited liability, which is owned as to 50 per cent. by Ms. Lee and 50 per cent. by Ms. Leelalertsuphakun. Ms. Lee and Ms. Leelalertsuphakun are sisters.

2. Dynamic Achieve is a company incorporated in BVI with limited liability, which is owned as to 50 per cent. by Ms. Lee and 50 per cent. by Ms. Leelalertsuphakun. Ms. Lee and Ms. Leelalertsuphakun are sisters.

3. High Knowledge is a company incorporated in BVI with limited liability, whose entire share capital is beneficially owned by Ms. Lue, who is the sister-in-law of each of Ms. Lee and Ms. Leelalertsuphakun.

4. Techfarm is a company incorporated in BVI with limited liability, whose entire share capital is beneficially owned by Ms. Yu Wa, an independent third party not connected with any of the chief executives, directors, management shareholders, substantial shareholders of the Company or their respective associates.

5. Zengen is a company incorporated in the United States, whose entire share capital is owned by independent third parties not connected with any of the chief executives, directors, management shareholders, substantial shareholders of the Company or their respective associates.

MISSION

The aim of the Group is to become a successful biopharmaceutical group in the PRC providing innovative and high quality pharmaceutical products of value that combat diseases, in particular, for the treatment of cardiovascular diseases, stroke, viral-infected sexual diseases, cancer and vaginitis, and improve health. The Directors believe that the Group can accomplish its mission by:—

- focusing on patients' needs by caring for the genuine interest and welfare of the customers;

- making use of its medical and scientific research results for practical applications;

- having the support of its knowledgeable, experienced and professional management team with innovative spirit and strong research and development capabilities; and

- increasing the market share of its products through its existing marketing and distribution network in the PRC.

COMPETITIVE STRENGTHS

The Directors believe that the Group has the following strengths over most of its competitors in the pharmaceutical industry in the PRC in particular:

- the Group's possession of three in-house developed technologies, namely (i) the snake venom technology, (ii) the low molecular weight heparin technology, and (iii) the water-based gel delivery system provides a technology platform for the future business development of the Group, based on which the Group's pipeline of new products are gauged;

- the Group's successful launch of three self-developed biopharmaceutical products for the treatment of stroke, cardiovascular diseases and viral-infected sexual diseases in the PRC has enabled the Group to position itself to take up a share in the biopharmaceutical markets in the PRC for such diseases and has enhanced customers' awareness of the Group's products;

- the Group's proprietary intellectual property in respect of its self-developed snake venom technology and topical interferon in water-based gel delivery form for viral-infected sexual disease have enhanced the Group's competitiveness in the biopharmaceutical industry in the PRC;

- the Group's two GMP-compliant pharmaceutical manufacturing workshops providing a quality assurance of the Group's products and an entry barrier for competitors in the PRC without GMP certification. As of 26th July, 2001, only 321 out of a total of 450 workshops for the production of lyophilized powder for injection and a total of less than five workshops for the production of gel nationwide in the PRC have been GMP certified;

- the Group's experienced dynamic and professional management team enables the Group to meet and respond quickly to the customers' needs and the challenges of the biopharmaceutical industry both in the PRC and overseas;

- the Group's scientific advisory board comprises 5 members who are mainly leading researchers from universities and research institutes in Hong Kong and the PRC has enabled the Group to have better access to the latest technological development in the biopharmaceutical field and, thus, to be better positioned to incorporate such development and technology in practical applications to meet the customers' needs and expectations. The board serves (i) to assist the Group in its overall research and development activities; (ii) to guide and evaluate the progress made by the Group on development projects; and (iii) as well as to provide strategic direction to the Group's research projects;

- the Group's research and development team which has been working closely with the universities and research institutions in the PRC and Hong Kong (namely 中國藥科大學 (China Pharmaceutical University), 中國藥品生物製品檢定所 (China Drug Evaluation Institute) and the Biological Research Institute of Hong Kong University of Science and Technology) to leverage on their strengths in carrying out pre-clinical studies of new products of the Group;

- the Group's strategic partnership with Zengen, a biotechnological company based in the United States enables the Group to have access to the latest information and development on biotechnology and biopharmaceutical products in the United States;

- the Group's effective and efficient distribution and marketing channels for its products in the PRC provides comprehensive marketing and distribution coverage of its products in the PRC;

- the Group's reputable brandname of "ZHAOKE" promotes customers' awareness given its market presence in the PRC since 1997; and

- the strong support and recognition from various PRC governmental authorities on the Group's business and products enables the Group to well position itself in the biopharmaceutical industry in the PRC.

AWARDS

The Group has obtained the following awards:

自然科學獎二等獎 (Second Prize in Natural Science)

In November 1994, 尖吻蝮蛇毒的生物化學研究 (Study of enzyme from snake venom of Agkistrodon Acutus) undertaken by Zhaoke was accredited 自然科學獎二等獎 (Second Prize in Natural Science) by 中國科學院 (Chinese Academy of Science). According to the Directors, the criteria for being selected as Second Prize in Natural Science is that the research must demonstrate superior scientific merit.

高新技術企業認定證書 (High-tech Enterprise)

In September 1995, Zhaoke was accredited as 高新技術企業 (New High Technology Enterprise) by 安徽省科學技術委員會 (Anhui Province Science and Technology Committee). According to the Directors, one of the criteria for being selected as a New High Technology Enterprise is that the enterprise must engage in one or more of the new high technologies prescribed by the State Ministry of Science and Technology.

國家級火炬計劃項目證書 (National Torch Project)

In March 1996, Zhaoke was accredited by 國家科學技術委員會火炬計劃辦公室 (State Science and Technology Committee of the PRC), now known as 科學技術部 (Ministry of Science and Technology), to undertake a national project of 國家級火炬計劃 (National Torch Project) for the development and commercialisation of Defibrase. According to the Directors, the criteria for being selected as one of such projects is that the project must demonstrate its scientific merit and its potential contribution to the advancement of science and technology.

外商投資先進技術企業 (Foreign Investment Advanced Technology Enterprise)

In April 1999, Zhaoke was accredited as 外商投資先進技術企業 (Foreign Investment Advanced Technology Enterprise) by MOFTEC. According to the Directors, the criteria for being selected as a Foreign Investment Advanced Technology Enterprise is that the enterprise must be an entity with foreign investment which must be in advanced technology areas.

1999 年國家重點技術創新項目 (Key National Technology and Innovation Project for the year 1999)

In June 1999, Declotana, a new product of the Group under research and development, was approved as 1999 年國家重點技術創新項目 (Key National Technology and Innovation Project for the year 1999) by 中華人民共和國國家經濟貿易委員會 (State Economic and Trade Commission of the PRC). According to the Directors, the criteria of being selected as key National Technology and Innovation Project is that the project must demonstrate its scientific merit as well as commercial viability.

2001 Hong Kong Innovation and Technology Fund Matching Grant

In May 2001, the Group has been awarded a matching grant of HK$1.38 million by the Hong Kong Government's Innovation and Technology Fund for the Group's project "Screening of Human Heparanase Inhibitors as Anti Cancer Drugs from Traditional Chinese Medicine" which is in cooperation with the Biological Research Institute of the Hong Kong University of Science and Technology.

PRODUCTS

As at the Latest Practicable Date, the Group has obtained valid production permits in the PRC to manufacture the following products:

Product name	Generic name	Approval number	Medical category	Dosage form	Medical application	Launch date	Technology used
ZHAOKE Defibrase	Defibrase (降纖酶)	衛藥准字 (Weiyaozhunzi) XF-0032 號	Category 4 chemical product *(note)*	Lyophilized powder for injection use (凍乾粉針劑)	Treatment for cerebral ischemic stroke (腦中風)	October 1997	Shake venom
ZHAOKE Livaracine	Low molecular weight heparin calcium (低分子量肝素鈣)	衛藥准字 (Weiyaozhunzi) X-187 號	Category 4 chemical product *(note)*	Lyophilized powder for injection use (凍乾粉針劑)	Treatment for heart disease and other cardiovascular (心血管) diseases	July 1998	Low molecular weight heparin
ZHAOKE Yallaferon	Topical interferon (干擾素)	國藥准字 (Guoyaozhunzi) S20010054	Category 4 biopharmaceutical product *(note)*	Topical gel (凝膠劑)	Treatment for viral-infected sexual disease	July 2001	Water-based gel delivery

Note: Please refer to "Industry Overview" for details.

Defibrase

ZHAOKE Defibrase is a protein extracted and purified using in-house proprietary method from snake venom of Agkistrodon Acutus with enzymatic activity. Defibrase has the pharmacological effect of reducing the chance of blood clot in stroke patients by reducing the elevated level of fibrinogen in stroke patients and facilitates the dissolution of fibrin clot. Defibrase has proven to help patients to improve and recover from neurological syndromes and disability of stroke (i.e. loss of speech, arm or leg movement) and accelerate functional recovery. Defibrase has been found to be effective and safe on treatment of stroke patients. ZHAOKE Defibrase is for intravenous injection use under the instruction of a qualified physician. It is necessary to store ZHAOKE Defibrase under the temperature of ten degree Celsius before use. ZHAOKE Defibrase is a product manufactured in the PRC that has successfully completed a 700-patients nationwide clinical trial organised by Chinese Medical Association in January 1999 to demonstrate the beneficial effects of Defibrase on stroke patients. The clinical results were presented in 1999 American Heart Association Scientific Session, an annual scientific meeting for worldwide cardiovascular professionals. In May 2000, Journal of American Medical Association, a leading international medical journal, published the results of a 500-patients double blind clinical trial on a five-year horizon conducted in North America, showing reduction of fibrinogen as a safe and effective treatment for ischemic stroke patients.

Livaracine

Livaracine is a low molecular weight heparin calcium (低分子量肝素鈣) obtained by chemical hydrolysis of un-fractionated heparin sodium. As different manufacturers have their own manufacturing processes, every low molecular weight heparin available for sale in the market is different with different specific activity and other chemical and physical properties. ZHAOKE Livaracine has successfully completed a 200-patient clinical trial organised by Anhui Provincial Hospital in Feburary 1997 and a 50-patient clinical trial organised by 北京協和醫院 in December 1997. Livaracine in lyophilized powder form can be preserved under room temperature without adding any preservatives with a shelf life of two years under normal storage condition. Livaracine is for deep subcutaneous injection under the instruction of a qualified physician. Livaracine was initially developed as an anticoagulant for use in the prevention and treatment of hyper-coagulation diseases such as deep venous thrombosis and in the prevention of clotting during haemodialysis. However, during the past few years, low molecular weight heparin has become a standard treatment for acute coronary syndromes, in particular, on unstable angina and myocardial infarction. In addition, it has been applied on ischemic stroke patients with hyper-coagulation conditions.

For the past two years, evidence for low molecular weight heparin's utility in the treatment of auto-immune diseases and cancer has been growing which is independent to its anticoagulation activity. Administration of low molecular weight heparin not only reduces secondary metastases of the primary tumor, but through an unexpected anti-angiogenic effect, it will also significantly reduce the growth of the primary tumor as well as the associated growth of the few secondary metastatic tumors that do occur. For auto-immune diseases, low molecular weight heparin has anti-inflammation activities through its inhibition of Heparanase. The Directors believe that the market potential of Livaracine will be tremendous in light of its expanding indications under intensive study.

Yallaferon

Yallaferon is a proprietary preparation of interferon (干擾素) for topical use developed by the Group's research team. Yallaferon is for the treatment of condyloma acuminata (genital warts, being a kind of wart) and other superficial viral infections such as herpes (疱疹). As a protein in nature, the activity of interferon can only be stabilised in lyophilized powder form at a range of 2 to 8 degree Celsius for a sustained period of time. To be stable for a meaningful period of time at room temperature, right stability agent must be selected for proper interaction with the protein. Moreover, interferon in gel formulation must be in state of readily disassociation from the gel base to ensure that it can effectively cross the skin barrier to the designated sites with a local concentration high enough to carry out effective treatment. ZHAOKE Yallaferon has successfully completed a 141-patient clinical trial organised by 北京醫科大學第一醫院 in August 1999. Prior to the launch of ZHAOKE Yallaferon, the available route of administration of interferon for treatment of viral infection is by way of injection only. However, for diseases, such as genital warts, which is superficial and spot-focused in nature, it is difficult to apply high enough concentration of interferon locally by way of systemic injection without causing significant side effects. ZHAOKE Yallaferon, which is in gel form, can be applied locally and directly to the infection site. Echoed with the relevant endorsement by Anhui Province Drug Administration in the form of public advertising materials, the Directors believe that ZHAOKE Yallaferon which is produced in topical gel form is the first of its kind in the PRC produced for commercial use for the treatment of genital warts as at the Latest Practicable Date.

Zhaoke's products, Defibrase, Livaracine and Yallaferon, are all biopharmacetical products. As advised by the Directors, Defibrase and Livaracine fall within sub-category (2) of Category 4 chemical products and Yallaferon, falls within sub-category (3) of Category 4 biopharmacetical products. Defibrase and Livaracine are subject to an administrative protection period of three years according to the then regulation effective before 1st May, 1999. Whilst the protection periods of Defibrase and Livaracine had expired in February 2000 and May 2001 respectively, Yallaferon has been granted a protection period for six years which will expire in October 2006 based on the relevant regulation effective after 1st May, 1999.

In addition, the Group has also been developing a number of pharmaceutical products, which are undergoing various phases of clinical examinations, trials and reviews by the relevant supervisory authorities as set out in the section headed "Research and development".

PRODUCTION

Production facilities

Zhaoke is the Group's manufacturing arm. In the early days after its establishment until August 1998, Zhaoke carried out its research and development, and manufacturing activities in the campus of USTC. To cope with the organic growth and the further expansion of the Group's business, the Group invested in building a new manufacturing plant in New and High Technology Industrial Development Zone of Hefei, Anhui Province, the PRC in 1997. The manufacturing plant was built in accordance with GMP requirements which govern and standardise the design and integration of equipment, process and support utilities. The new manufacturing plant was completed and came into operation in August 1998. The existing

manufacturing plant occupies a total gross floor area of approximately 3,021 sq.m. comprising two production workshops for the production of topical gel and lyophilized powder for injection, a warehouse and ancillary offices for administration and finance functions. The manufacturing plant is also equipped with a molecular laboratory, a protein chemistry laboratory and a synthetic chemistry laboratory for quality control and research and development purposes. Zhaoke was awarded with the Certificates of GMP for Human Drugs issued by the SDA for its workshop on the production of bulk pharmaceutical for injection (注射用原料藥) and lyophilized powder for injection (凍乾粉針劑) in September 1999 for a period of five years expiring on 20th September, 2004 renewable thereafter and for its workshop on the production of recombinant human α-2b interferon in gel in May 2001 for a period of one year expiring on 22nd May, 2002 renewable thereafter. The GMP license for the gel workshop will be renewed, subject to the review by SDA upon expiry, for a new license which will be valid for another five years thereafter. The manufacturing plant has a current annual production capacity of manufacturing up to 1.3 million vials of lyophilized powder for injection use and up to 10 million tubes gel for topical use. Currently, the Group's production facilities for lyophilized powder for injection use and topical gel are operating at about 90 per cent. and 20 per cent. respectively of the total available capacity. The Directors believe that there is room for the Group to increase its production output of its products in the near future. Since its establishment, Zhaoke has obtained all the required permits and certificates issued by the relevant authorities in relation to its pharmaceutical manufacturing business in the PRC.

Production planning

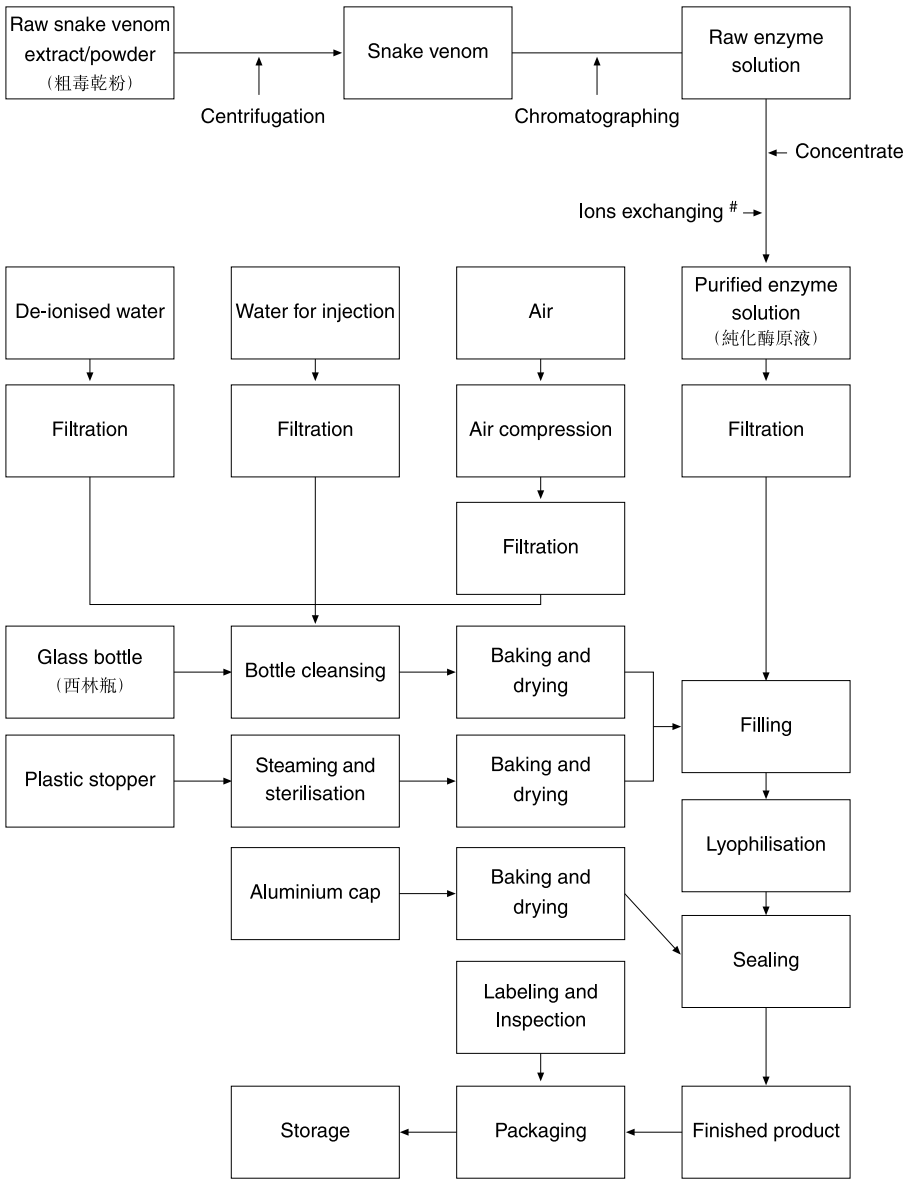
The Group formulates its production plans primarily according to market demand. The monthly production volume of each product is preliminarily determined on a yearly basis in advance by reference to the anticipated market demand and sales orders on hand which will be adjusted according to actual demand and stock level on a monthly basis. The Group had negligible slow-moving finished goods during the Track Record Period.

Production processes

The production processes of the Group's products are handled through a team of workers with extensive use of specialised machinery and equipment and apparatuses. In order to ensure a high quality for its products, the Group has imported key equipment for production from overseas, namely, advanced lyophilisation machinery from United States for lyophilisation process, purification system from Sweden for purification process, and precise filling machine from Italy for filling process.

The following diagrams summarise the major steps in the production of the Group's products:

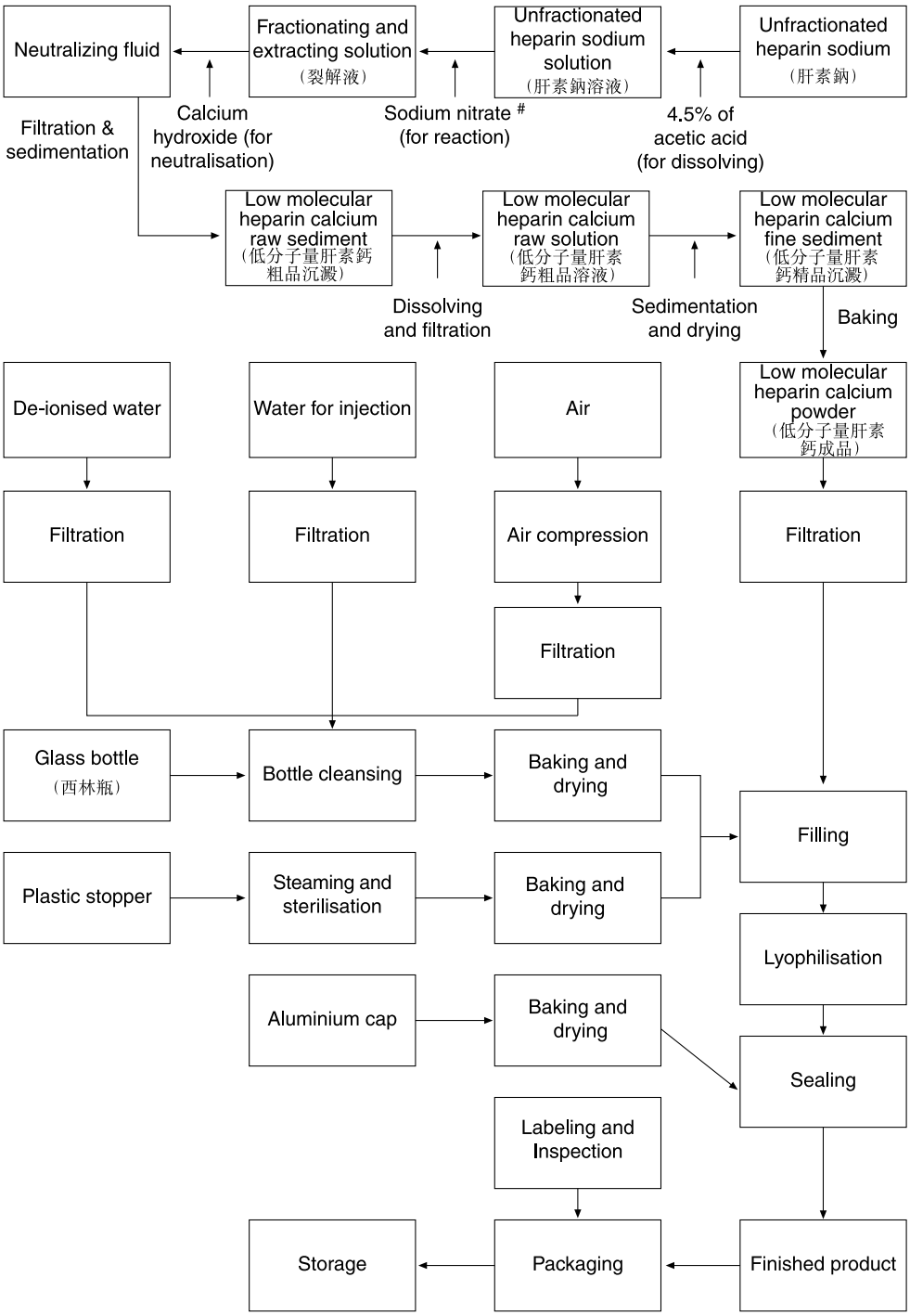
1. Production process for Defibrase:



: proprietary technology applied

One of the production characteristics of Defibrase is that it cannot be sterilised by high temperature, otherwise its efficacy will be reduced. Therefore, it has to be produced in bacteria-free level at 10,000 environment during purification and filling is carried out in bacteria-free level at 100 *(Note)*.

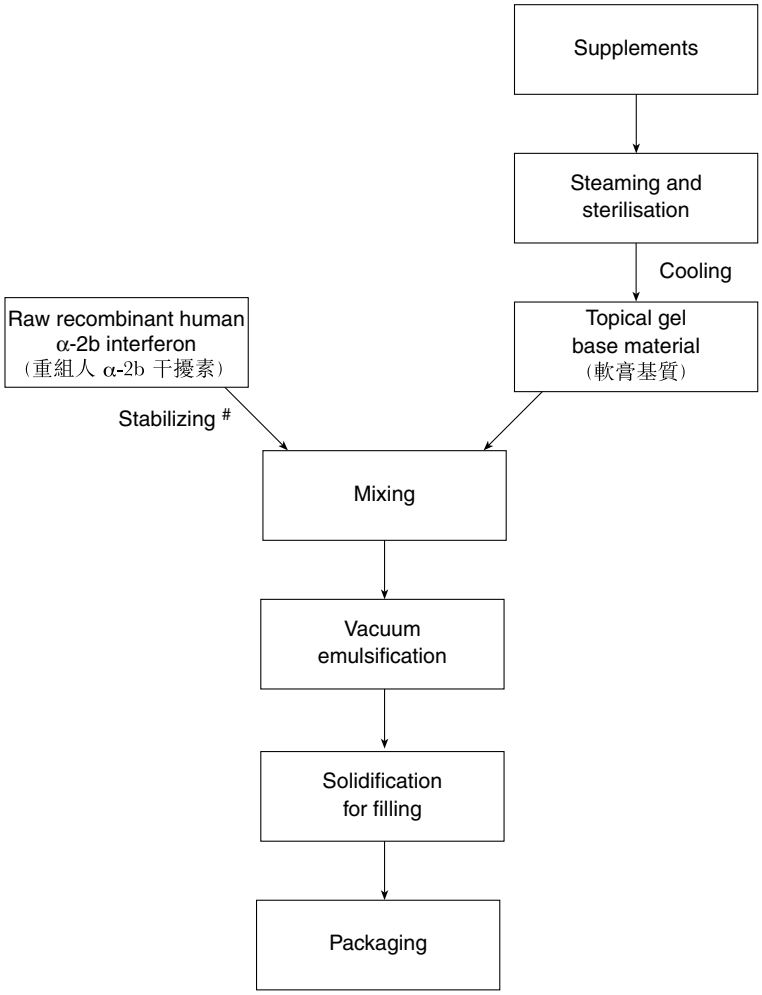
2. Production process for Livaracine:



: proprietary technique applied

Low molecular weight heparin calcium is prepared in bacteria-free level at 100,000 environment and filling is carried out in bacteria-free level at 100 *(Note)*.

3. Production process for Yallaferon:



: proprietary technology applied

Note:

The table below sets out information regarding bacteria-free levels:-

	Amount of dust/m³		**Amount of live microorganism/m³**	
Bacteria-free level	with size ≧0.5 μm	with size ≧5 μm	Subsiding bacteria	Floating bacteria
at 100	≦3,500	0	≦1	≦5
at 10,000	≦350,000	≦2,000	≦3	≦100
at 100,000	≦3,500,000	≦20,000	≦10	≦500

RAW MATERIALS

The Group mainly sources its raw materials such as interferon, glass bottle, rubber cap and packaging material from domestic suppliers in the PRC. Samples of the raw materials are sent to the quality control department for testing upon receipts to ensure the quality of the raw materials is in accordance with the requirements set by Zhaoke and the relevant laws and regulations. For the year ended 31st December, 2001, approximately 43 per cent. of the total purchases are payable on credit with a credit term of 90 days in general while approximately 57 per cent. of the total purchase are on a cash-on-delivery basis. For the year ended 31st December, 2001, all purchases are settled in Renminbi by cash (approximately 20 per cent. of the total purchase), cheque (approximately 10 per cent. of the total purchase) or telegraphic transfer (approximately 70 per cent. of the total purchase). For each of the three years ended 31st December, 2001, the cost of raw materials (such as un-fractionated heparin sodium, raw supplements and raw snake venom extracts and other organic or inorganic reagents) accounted for approximately 6.8 per cent., 14.8 per cent. and 24.9 per cent., respectively of the total cost of sales of the Group whilst the cost of packaging materials (such as bottles, paper, rubber stoppers and aluminum caps) accounted for approximately 3.7 per cent., 8.5 per cent. and 13.0 per cent., respectively, of the total cost of sales of the Group.

Other than the supply of raw recombinant human α-2b interferon, the Group has not entered into any long term supply contracts with suppliers of the Group in order to maintain flexibility in sourcing quality supplies at competitive prices. The Group elected to enter into long-term supply contracts of raw recombinant human α-2b interferon from a particular supplier because it is a compliance requirement in obtaining the production permit of Yallaferon that a stable supply of such raw material with consistent high quality has to be secured by the Group. Given the vast number of market participants, the Directors do not anticipate that the Group will have any material difficulties in sourcing its raw materials and packaging materials from other suppliers. The supplier of raw recombinant human α-2b interferon was the second largest supplier of the Group for the year ended 31st December, 2001. The purchase from this supplier was approximately 12.7 per cent. of the total purchases.

For each of the three years ended 31st December, 2001, purchases from the five largest suppliers of the Group accounted for approximately 52.0 per cent., 70.4 per cent. and 63.9 per cent., respectively, of the Group's total purchases. For the year ended 31st December, 2001, the largest supplier of the Group was 常州生化纖紅製藥有限公司. For each of the three years ended 31st December, 2001, the largest supplier of the Group accounted for approximately 15.6 per cent., 26.7 per cent. and 22.9 per cent., respectively of the Group's total purchases. The Group has established business relationships with its five largest suppliers for a period ranging from one year to three years and the average length was approximately two years. None of the Directors, their associates or any significant shareholder of the Company (who or which to the best knowledge of the Directors owns more than five per cent. of the issued share capital of the Company) has any interest in any of the Group's five largest suppliers during the Track Record Period.

INVENTORY CONTROL

In order to ensure an adequate supply for production, it is the general policy of the Group to maintain inventory of raw materials and other essential packaging materials to the extent of not more than three month's average sales requirement.

In order to minimise the occurrence of obsolete stocks, the Group implements stock control procedures concerning matters such as budgeting production, sales, accounting and

warehouse information. The inventory records of the Group are kept up-to-date to reflect actual movements of inventory. In determining whether a provision for obsolete inventory is required, the Group takes into consideration the physical state and the degree of utilisation or realisation of the inventory.

QUALITY CONTROL

The Group is fully committed to maintain a high standard of quality control for its production. Zhaoke has been granted with the Certificates of GMP for Human Drugs in respect of its production of bulk pharmaceutical for injection (注射用原料藥) and lyophilized powder for injection (凍乾粉針劑) in September 1999 and in respect of its production of recombinant human α-2b interferon (gel) in May 2001. The Group has set out a quality control standard for its pharmaceutical products, which is in line with the quality control standard approved by SDA.

The quality control department of the Group is responsible for monitoring the entire manufacturing processes of the Group and maintaining the high quality of the Group's finished products on a consistent basis. As at the Latest Practicable Date, the quality control department of the Group has 14 staff with extensive experience in the biopharmaceutical industry. The quality control department of the Group not only conducts regular tests on samples of incoming raw materials, work-in-progress, workshop environment, water quality, finished products and packaging materials, but also ensures that the entire production process is carried out in strict compliance with the GMP requirements and standards.

During the Track Record Period, the Group did not experience any failure in the quality control of its products which could have caused any material interruption to the Group's business. The Directors have confirmed that none of the products manufactured by the Group have been suspended for production by the relevant regulatory authorities in the PRC since the commencement of their production. The Directors have also confirmed that the Group has not received any claims, lawsuits or litigation concerning the quality of its products. It is the Group's policy to keep a certain amount of each batch of the Group's ex-factory products as samples for a period of one year plus the effective period of two years or 18 months (as the case may be) for testimonial and sample verification purpose in case of any possible claims arising from application of such products. To ensure the integrity and the accountability function, the quality control department reports directly to the Managing Director of the Group.

SALES AND MARKETING

Sales and distribution

All pharmaceutical manufacturing enterprises in the PRC can only sell their pharmaceutical products to enterprises holding a "藥品經營企業許可證" (Pharmaceutical Trading Enterprise Permit) according to the "藥品流通監督管理辦法(暫行)" (Provisional Measures regarding the Supervision and Administration of the Circulation of Pharmaceutical Products) published by SDA on 15th June, 1999. Accordingly, the Group sells its pharmaceutical products to hospitals and retail pharmaceutical shops through distributors in the PRC holding the "藥品經營企業許可證" ("Pharmaceutical Trading Enterprise Permit"). Currently, the Group's sales and distribution network is divided into three major districts covering approximately 28 provinces, cities or districts and 500 hospitals and clinics in the PRC. The Group carries out its sales and distribution activities through Zhaoke's sales offices located in Guangzhou and Hefei, the PRC. These sales offices, together with branch offices in Beijing and Shanghai, are responsible for marketing and after-sales services in a designated region arranged in advance

by the chief marketing officer of the Group. Other than liaisons with the distributors and end-users, the marketing activities (including implementation of the regional advertising and promotional activities, such as seminars, conferences and health consultation) are conducted by sales and branch offices of Zhaoke. Sales offices and branch offices are on lease or owned.

The map below illustrates the geographical presence of the Group's sales and marketing activities through (i) establishment of collaborative arrangements with the Group's distributors or (ii) the Group's own sales force in the PRC:

Distribution network of the Group

Note: "Shanghai district" refers to area covered by the staff of the Shanghai representative office.
"Guangzhou district" refers to area covered by the staff of the Guangzhou sales office.
"Beijing district" refers to area covered by the staff of the Beijing representative office.

The table below sets out a analysis of the turnover breakdown of the Group's products during the Track Record Period:

Major district	Year ended 31st December, 1999		2000		2001	
	HK$'000	*%*	*HK$'000*	*%*	*HK$'000*	*%*
Beijing district[1]	1,552	24.8	3,793	55.3	5,914	57.2
Shanghai district[2]	4,051	64.8	2,115	30.9	2,669	25.8
Guangzhou district[3]	650	10.4	944	13.8	1,763	17.0
Total	6,253	100.0	6,852	100.0	10,346	100.0

Notes:

1. Beijing district — Beijing, Gansu, Hebei, Heilongjiang, Henan, Inner Mongolia, Jilin, Liaoning, Ningxia Huizu Autonomous region, Qinghai, Shaanxi, Shanxi, Tianjin and Xinjiang Uygur Autonomous region

2. Shanghai district — Anhui, Hubei, Jiangsu, Shandong, Shanghai and Zhejiang

3. Guangzhou district — Fujian, Guangdong, Guangxi, Guizhou, Hainan, Hunan, Jiangxi, Sichuan and Yunnan

Type of customers	Year ended 31st December, 1999		2000		2001	
	HK$'000	*%*	*HK$'000*	*%*	*HK$'000*	*%*
Hospitals	2,368	37.9	1,874	27.3	1,478	14.3
Distributors	3,885	62.1	4,978	72.7	8,868	85.7
Total	6,253	100.0	6,852	100.0	10,346	100.0

During the Track Record Period, all the Group's products were sold in the PRC. The sales were denominated in RMB. During the Track Record Period, the customers of the Group mainly comprised pharmaceutical product distributors and hospitals in the PRC, which are third parties independent of any members of the Group, the Directors, the Initial Management Shareholders and their respective associates. The Group has established an average of two years relation with the majority of its customers.

For each of the three years ended 31st December, 2001, sales to the five largest customers of the Group's business accounted for approximately 29.2 per cent., 36.9 per cent. and 27.5 per cent., respectively, of the Group's total turnover. For each of the three years ended 31st December, 2001, the largest customer of the Group accounted for approximately 8.4 per cent., 16.7 per cent. and 9.7 per cent., respectively, of the Group's total turnover. The Group has established business relationship with some of its five largest customers for more

than two years. None of the Directors, their associates or any significant shareholder of the Company (who or which to the knowledge of the Directors owns more than five per cent. of the issued share capital of the Company) has any interest in any of the Group's five largest customers during the Track Record Period.

Sales representatives and distributors

Sales representatives

The chief marketing officer of the Group, who is also the sales manager of the Guangzhou sales office, together with two regional sales managers supervise the sales and distribution network of the Group and the activities of each of the branch offices. As at the Latest Practicable Date, the Group had a team of 25 full-time sales representatives, all of them were strategically located at the three offices in Beijing, Shanghai and Guangzhou. The sales office in Hefei is located at the manufacturing plant of the Group and is mainly for the provision of supporting services to the three regional offices of the Group. The principal duties of the sales representatives of Zhaoke are to maintain the business relationship with the existing customers and the distributors of the Group, liaise with prospective customers and distributors, coordinate the delivery of the Group's products, follow up on the after-sales services and the remittance of sales proceeds. The Group has a policy of arranging training for its sales and marketing staff on the general knowledge of the pharmaceutical industry in the PRC and the nature and therapeutic effect of the Group's pharmaceutical products from time to time.

To motivate the performance of its sales representatives, commencing from January, 2002 onwards Zhaoke has introduced a floating compensation system (浮動工資制) pursuant to which each sales representative is requested to submit an annual sales target every year to the relevant branch office, which will then be forwarded to the sales head office of Zhaoke for consideration and approval. Monthly salary of the sales representatives varies depending not only on the extent of sales target achieved, but also on other factors such as cost control, the length of the collection period of the sales proceeds and etc. This compensation system is aimed at best motivating the Group's sales team.

Distributors

Apart from deploying the Group's own sales force, in an effort to facilitate and enhance the sales coverage to hospitals and clinics in various provinces of the PRC, a number of regional wholesalers are appointed by the Group as distributors, with which Zhaoke has entered into a distribution agreement whereby the relevant distributor undertakes to purchase at their own risk a certain amount of the product of the Group on an annual basis for their own onward marketing and sales ultimately to hospitals and clinics as end-users. The products of the Group are offered to the distributors at different terms based on terms and conditions of their respective distribution agreements with the Group. In order to enable the Group to maintain flexibility and to respond to the changing market conditions, the Group sets sales target in such distribution agreement for the distributors. In the event that these distributors cannot meet the sales target, the Group has discretion to terminate the relevant distribution agreement.

As at 31st December, 2001, Zhaoke had a total of 49 distributors in the PRC. For each of the three years ended 31st December, 2001, turnovers derived from the sales to these distributors accounted for approximately 62.1 per cent., 72.7 per cent. and 85.7 per cent., respectively. The Group recognised its turnover at the time when the products were delivered to and accepted by the distributors of the Group.

Internal control on credit and cash receipt

The Group carries out its sales both on the basis of open accounts and on the basis of cash on delivery. For the former basis, the Group normally grants credit terms of a range from 30 to 180 days to customers (including distributors) regarded as creditworthy by reference to their historical payment records and sizes. Customers with better credit history and of larger sizes will get longer payment term. The rest of the sales of the Group are settled in cash, bank cheques or telegraphic transfer on delivery. The Group also grants few credit terms of more than 180 days to existing active customers. The following table illustrates the breakdown of credit policy of the Group for the Track Record Period:

	Year ended 31st December,		
	1999	**2000**	**2001**
	%	*%*	*%*
Cash on delivery	2.0	3.7	32.3
Open accounts	98.0	96.3	67.7
Total	**100.0**	**100.0**	**100.0**

The Group has implemented a credit control system to monitor the extension of credits to its customers. Normal credit policies are formulated by the marketing manager based on certain criteria such as creditability of customers, product nature and the financial position and cash flow of the Group and reviewed by the Directors regularly. Normal credit lines are approved by the marketing manager. Any extension from normal credit line being granted to a particular customer would be initiated by the marketing manager and approved by the Directors. Aged account receivables are reviewed regularly in order to identify problem accounts at an early stage. Following the identification of any doubtful debts, provisions are made by the Group on a specific basis by the Directors in accordance with the Group's accounting policy. For the year ended 31st December, 1999 and 2000, for debtors who have not traded with the Group for more than one year, 50 per cent. provisions were made for debts overdue for more than one year and 100 per cent. provision were made for debts overdue for two years or above. For the year ended 31st December, 2001 having considered the increase in the turnover of the Group, 50 per cent. provision was made on debts aged 180-365 days and 100 per cent. provision on debts overdue for more than one year. The account receivables, net of provision for bad debts, of the Group as at 31st December, 2001 was HK$2,435,000 (out of which as to (i) approximately HK$1,250,000 was aged 1-90 days, (ii) HK$613,000 was aged

91-180 days, (iii) HK$416,000 was aged 181-365 days, and (iv) HK$156,000 was aged over 365 days and under 3 years), with subsequent settlement up to 30th April, 2002 amounting to HK$1,518,000. The bad debts of the Group for each of the three financial years ended 31st December, 2001 are as follow:

	Year ended 31st December,		
	1999	**2000**	**2001**
	HK$'000	*HK$'000*	*HK$'000*
Bad debts written off	167	369	312
Specific provision	85	102	—
General provision	—	—	440
	252	471	752

Marketing and advertising activities

The sales and marketing department of the Group is also responsible for the formation and implementation of the marketing strategies of the Group. It performs market analysis and coordinates promotional activities to enhance the market presence and acceptance of the Group's products. Nationwide advertising and promotional activities are planned and implemented by the sales and marketing department of Zhaoke whereas each sales and branch office coordinates the local advertising and promotional activities within its region. On the other hand, the distributors appointed by the Group will also conduct, at their own costs, local advertising and promotional activities with assistance from Zhaoke as and when requested.

For each of the three years ended 31st December, 2001, advertising and promotion expenses incurred by the Group amounted to approximately HK$1.5 million, HK$1.6 million and HK$2.7 million, respectively, representing approximately 24.0 per cent., 23.8 per cent. and 26.3 per cent., respectively, of the Group's total turnover.

After-sales services

Recognising the importance of the feedback from its customers, the Group places great emphasis on its after-sales services. The sales and marketing staff of the Group is responsible for the follow-up actions after its sales to ensure that its customers fully understand the applications of the Group's products and to obtain feedback from the customers on their requirements and preferences. Every sales representative is required to report any severe adverse reaction or other quality problem caused by the Group's products immediately to the regional manager who will then prepare a detailed report for the attention of the management within three days of the occurrence of the incident. Such report will be followed up by the quality control department, research and development department and senior management of the Group so that any problem can be resolved in time and new drug applications or forms can be developed and improvements on products can be made to suit their needs.

Website

To take advantage of the information technology development, the Directors has developed a website for the Group under the domain name of www.zhaoke.com with a primary objective of promoting the Group's products and providing the latest medical information on diseases which the Group's pharmaceutical products are targeted to combat.

RESEARCH AND DEVELOPMENT

Zhaoke was accredited as a 高新技術企業 (New High Technology Enterprise) by 安徽省科學技術委員會 (Anhui Province Science and Technology Committee) in September 1995 and a 外商投資先進技術企業 (Foreign Investment Advanced Technology Enterprise) by MOFTEC in April 1999. The Directors reckon that product research is one of the fundamental and critical factors for the growth and success of the Group. As at the Latest Practicable Date, the research and development department of the Group comprises of a total of seven specialists, five of which have been awarded bachelor degree or above and all of them are very experienced in clinical experiment research and product development.

In-house research and achievements of the Group

The research and development department of the Group has been conducting in-house research in the fields of molecular biology, biochemistry, pharmacology and chemical synthesis by using advanced and state-of-the-art instruments and devices in the research laboratories located at Zhaoke. Over the years of its in-house research efforts since the establishment of Zhaoke in 1994, the research and development department of the Group has on its own developed three technology platforms, namely (i) the snake venom technology (which was built with reference to and based on the technology of protein extraction and purification from snake venom with enzymatic activities injected by the PRC partner into Zhaoke in 1994), (ii) the low molecular weight heparin technology, and (iii) the water-based gel delivery system. The research and development department of the Group has particular focus in identifying new indications and new applications for the Group's existing products. At present, the core areas of the Group's research and development department lie in the areas of (i) cardiovascular diseases and stroke, (ii) viral infection, (iii) cancer, and (iv) vaginitis.

(i) *Snake venom technology*

With reference to and based on the technology of protein extraction and purification from snake venom with enzymatic activities injected by the PRC partner into Zhaoke in 1994, the Group has successfully developed a proprietary technology means to extract the potential therapeutic proteins or peptides from snake venom, which are known to be effective of treating cardiovascular diseases. This proprietary technology contributes to the commercialisation of ZHAOKE Defibrase in late 1997. The Group's new developments of Declotana (a category 1 new drug and an application for clinical trial thereof has been submitted to the SDA in 1998) and of Hemocoagulase for injection (which is currently under pre-clinical study) are also based on this snake venom technology.

In October 1999, the Group was selected to give a presentation on the clinical results of ZHAOKE Defibrase in the 72nd Scientific Sessions of America Heart Association held in the United States, which proved to reflect the success of the Group's snake venom technology within the cardiovascular profession.

(ii) *Low molecular weight heparin technology*

The Group has successfully developed an in-house technique for making low molecular weight heparin based on the open low molecular weight heparin technology using commonly and readily available heparin as raw material, resulting in the contribution to the commercialisation of ZHAOKE Livaracine in mid 1998. The Directors intend to utilise this technology (i) to explore new dosage formulation (such as the oral and the topical gel forms which are found to be more convenient to administer) so as to pursue for new market segments, and (ii) to explore new indications for low molecular weight heparin (such as applying Livaracine to treat kidney-related diseases and skin diseases). According to the Directors, the low molecular weight heparin is derived from Heparin which is a natural product and therefore not patentable. However, the Group has been developing the process for making low molecular weight heparin efficiently and with constant quality. Therefore, although the molecule itself is not proprietary, the process is proprietary.

In February 1997 and December 1997, ZHAOKE Livaracine, which is the representative product of the Group's low molecular weight heparin technology, had successfully completed a 200-patient clinical trial organised by Anhui Provincial Hospital and a 50-patient clinical trial organised by 北京協和醫院 .

(iii) *Water-based gel delivery system*

The Group has also successfully developed a proprietary formulation for topical delivery of proteins or peptides. This is a unique formulation allowing macromolecules to penetrate the skin barrier of the human body to carry out the therapeutic effects locally. This proprietary technology contributes to the commercialisation of ZHAOKE Yallaferon, a topical interferon in July 2001. The Directors consider that the commercialisation of ZHAOKE Yallaferon was the first of its kind in the PRC for the treatment of genital warts. By adopting this technology, the Group is in the process of developing a new pharmaceutical product, an eye gel formulation for cornea ulcer, an application for clinical trial of which has been submitted to the SDA in 2000. Two other products, namely anti-fungus peptide and Livaracine, which is to be in topical gel formulation, is also under pre-clinical study.

In August 1999, ZHAOKE Yallaferon, which is the representative product of the Group's water-based gel delivery system, had successfully completed a 141-patient clinical trial organised by 北京醫科大學第一醫院 .

Association with outside research institutes

In addition to its own research efforts, the research and development department of the Group has collaborations with various reputable universities and research institutions both in the PRC and Hong Kong, namely 中國藥科大學 (China Pharmaceutical University), 中國藥品生物製品檢定所 (China Drug Evaluation Institute) and the Biotechnology Research Institute of the Hong Kong University of Science and Technology to leverage on their strengths in carrying out pre-clinical studies of new products of the Group.

The Group is also in co-operation with the Biotechnology Research Institute of the Hong Kong University of Science and Technology on "Screening of Human Heparanase Inhibitors as Anti-Cancer Drugs from Traditional Chinese Medicine", which is a process of identifying an inhibitor compound for heparanase, an enzyme with implications in cancer and autoimmune diseases. In May 2001, the project was awarded a matching grant of approximately HK$1.38 million from the Hong Kong Government's Innovation and Technology Fund. The Group will hold all the intellectual property rights arising from the project. The Group is a member of the steering committee and participates in reviewing the progress of the project from time to time. The Group is required to contribute approximately HK$1.38 million in total during the term of the project which is expected to end around mid 2004. Apart from this specific co-operation project with Hong Kong University of Science and Technology, the Group intends to examine the university's available technology such as the sustained release drug technology, pulmonary drug delivery system for macromolecules and liposome-based liver-targeted delivery system for possible licensing opportunity.

Furthermore, the Group has formed a strategic partnership with Zengen. As at the Latest Practicable Date, Zengen owns 2 patents issued in the United States and 1 patent issued in Europe and 6 patents in the United States, 3 patents in PCT countries and 2 patents in Japan pending-to-be-issued by relevant authorities on proprietary technologies (all are for treatment of inflammation and anti-infection of virus based on the peptide technology), with a view to licensing in certain proprietary technology for commercialisation in the PRC, Hong Kong and Taiwan. In particular, the Group has licensed Zengen's peptide technology for vaginitis for commercialisation, based on which the Group is prepared to apply for clinical trial of its developing product Anti-fugus peptide for treatment of uro-genital conditions that include infections, inflammation or both.

Scientific advisory board

The Company has established a scientific advisory board on 1st Feburary, 2002 to provide consultation services to the Board in relation to the overall research and development activities of the Group. The main duties of the scientific advisory board are to guide and evaluate the development progress of the research projects as well as to provide strategic direction to the Group's research.

The scientific advisory board meets once a year, although ad hoc meetings to focus on specific issues may also be convened. It is the intention of the Company to invite leading researchers and clinicians from universities and research institutes to sit on its scientific advisory board. As at the Latest Practicable Date, members on the scientific advisory board are:

Professor James Lipton	Chief Scientific Officer of Zengen *(Note)*
Professor Tsim Wah Keung, Karl (詹華強)	Associate Professor, Department of Biology, Hong Kong University of Science and Technology
Professor Hu Xueqiang (胡學強)	Chief Neurologist and Head of 中山大學附屬第三醫院神經科 (Neurology Department, Third Affiliated Hospital of Zhongshan Medical University of China)
Professor Fung Yuen Kai (馮元啟)	Associate Professor of School of Medicine of University of South California, Director of Clayton Molecular Biology Program of Children's Hospital of Los Angeles and President-elect (2002) of Association of Chinese Genetics in America USA
Professor Yong Mengwu (翁孟武)	Deputy director of 復旦大學醫學院皮膚病學研究所 (Research Institute of Dermatology, Fudan University, Medical Academy) and Chief Physician of 復旦大學醫學院華山醫院皮膚性病學教研室 (Department of Dermatology and Venereology, Hua Shan Hospital, Fudan University, Medical Academy)

Note:

Particulars of Zengen is set out below:

Background and business

Zengen is a company established in California, the United States on 18th May, 1999 focusing on discovering, developing and commercialising innovative products to treat and prevent infection and inflammation through application of its peptide technologies. These technologies are self-developed and are based on an extensive background of years of academic research on peptide molecules derived from Alpha-Melanocyte-Stimulating Hormone (α-MSH), an endogenous molecule that modulates inflammatory and immune responses.

Based on the available unaudited financial statements of Zengen, the total equity of Zengen was US$11.6 million as at 4th June, 2002.

Shareholders and their background

There are more than 100 shareholders of Zengen. Based on the available information form Zengen, shareholders of Zengen are US citizens.

There is no controlling shareholder in Zengen. The single largest shareholder holds about 16 per cent. of the total issued share capital of Zengen. Those shareholders of Zengen holding more than 5 per cent. of the total issued share capital of Zengen have an aggregate shareholding in Zengen of about 66 per cent.

Senior management and their background

There are at present a total of 14 staff in Zengen, some of whom are detailed as follows:—

R. Steven Davidson, Ph.D., MBA, president, CEO and director

Dr. Davidson has over eight years of experience in the biopharmaceutical industry. Dr. Davidson received his MBA in International Finance and Ph.D. in Biopharmaceutical Project Management from the American University of Asturias.

Matthew C. Lipton, JD, COO

From 1997 to 2001, Mr. Lipton was a partner at Browning & Lipton, a Texas law firm specialising in healthcare and corporate law. Mr. Lipton received his Juris Doctorate degree from Southern Methodist University in Dallas, Texas and his Bachelor's of Science degree in Psychology from Johns Hopkins University in Baltimore, Maryland.

Jo Ann L. Sevidal, CFO

Ms. Sevidal has over eight years experience as a controller and chief financial officer in the biopharmaceutical industry.

James M. Lipton, Ph.D., CSO and director

From 1966 to 2000, Dr. Lipton held positions, including professor of Physiology and Anesthesiology and Pain Management at the University of Texas - Southwestern Medical Center at Dallas, Texas. Dr. Lipton currently serves as Visiting Professor of Internal Medicine at the University of Milan Medical School in Milan, Italy. Dr. Lipton received his Ph.D. from the University of Colorado. He was awarded post-doctoral grants at the University of Michigan Medical School and a Special Research Fellowship at the Institute of Animal Physiology in Cambridge, United Kingdom. Dr. Lipton has more than 20 years experience in the pharmaceutical industry and has participated in numerous research projects funded by the National Institute of Health, the Department of Defense, health foundations and state governments.

Matthew Burns, Corporate Secretary and General Counsel

Mr. Burns was an associate attorney at law firms in Los Angeles and San Francisco respectively. His practice at both law firms concentrated on mergers and acquisitions and corporate finance for companies in a variety of industries, including life sciences and technology. Mr. Burns received his JD from Stetson University of College of Law in 1995 and his B.A. in Finance from the University of South Florida in 1992.

Terms of injection agreement

On 25th February, 2002, the Company (i) allotted and issued the then 5 per cent. of the enlarged shareholding in the Company to Zengen and (ii) agreed to pay an amount equal to the greater of a running royalty equal to 8 per cent. of net sales for licensed products sold by the Group (or its sublicensee) or 8 per cent. of any royalty payments the Group receives for net sales of licensed products from a sublicensee (in the event the Group elects to further license the rights granted thereto) in consideration of Zengen giving the Group an exclusive license to commercialise the licensed subject matter of peptides for treatment of uro-genital conditions in Hong Kong, Macau, PRC and Taiwan (excluding elsewhere) within 30 months from 2nd February, 2002.

Status of Group's development with Zengen's peptide technology

The peptide technology licensed to the Group by Zengen is for treating uro-genital conditions. The relevant patent application has been submitted on 23rd March, 2000 and the application is still under processing.

Most of the pre-clinical studies (such as biochemistry study, in-vitro and in-vivo pharmacology studies, acute toxicology, mutagenic study and formulation development) have been completed. The Directors believe that the peptide technology licensed from Zengen serves to leverage on the existing water-based gel delivery technology platform of the Group by blending and complementing each other in a synergical manner.

New product development

Research and development of the Group on new products are generally divided in various stages, being (i) performing technical feasibility study and analysis (pre-clinical study), (ii) obtaining relevant regulatory approvals for clinical trial, and (iii) undergoing various stages of clinical trials as required by the regulatory authorities. During the technical feasibility study and analysis stage, the Group conducts research on all aspects of the new product including its prescription/formula, toxicity, pharmacological and therapeutic effects, manufacturing process, quality and stability. After completion of the technical feasibility study and analysis stage, the Group will make an Investigational New Drug application submission to the relevant regulatory authorities (at both provincial and State levels) for approval. The regulatory approval stage generally includes a review by the regulatory authorities which is carried out in a form of expert committee on the submission which comprised the findings obtained in the technical feasibility study and analysis stage. After obtaining the regulatory approval, the Group will engage one or several principal investigators to conduct clinical trials based on samples of the new product in study sites approved by the regulatory authorities with an approved protocol. After completion of the clinical trial and a study report by the principal investigators, the Group will submit a New Drug Application to the SDA for review which is also carried out in the form of expert committee review. After the relevant approvals from the regulatory authorities for the New Drug Application and GMP certification for the workshop have been obtained, commercial production of the new products may then commence. Depending on the nature of the new products, the time required to bring the new product from research to production may vary.

Expenditure incurred on projects in the developing new products is capitalised and deferred only when the projects are clearly defined, the expenditure is separately identified and there is reasonable certainty that the projects are technically feasible and the products have commercial value. Product development expenditure which does not meet these criteria and research costs are expensed when incurred.

Deferred development costs are amortised, using the straight-line method, over the expected useful lives of the products, commencing in the year when the products are put into commercial production.

For each of the three years ended 31st December, 2001, the research and development cost incurred by the Group, which included laboratory materials, GMP software and other daily operating expenses of the research and development department, was approximately HK$0.8 million, HK$0.9 million and HK$2.1 million, respectively (of which as to HK$0.3 million, HK$0.1 million and HK$0.4 million were expensed and as to HK$0.5 million, HK$0.8 million and

HK$1.7 million were deferred), representing approximately 13.5 per cent., 12.8 per cent. and 20.7 per cent., respectively, of the total turnover of the Group. As at 31st December, 2001, the research and development cost deferred by the Group stood at HK$6.9 million, out of which as to HK$2.6 million was attributable to Yallaferon, HK$4.1 million to Declotana and the balance of HK$0.2 million to human heparanase inhibitor. The research and development cost so deferred have been amortised (as in the case of Yallaferon which is on sale) and will be amortised (as in the case of Declotana and human heparanase inhibitor which are under development) upon commercialisation of the pharmaceutical products. The amortisation period for each of Yallaferon, Declotana and human heparanase inhibitor were 6 years, 12 years and 12 years commencing from the date of commercialisation respectively. As a general policy, the Group intends to allocate and apply 10 to 20 per cent. of its budgeted annual turnover as the annual research and development expenses of the Group.

The Group's in-house research and development department has been actively involved in the research and development of the new products for the Group based on the existing three technology platforms and advice of professionals from outside institutions and the scientific advisory board.

The Group is prepared to apply for clinical trial of its developing product Anti-fungus peptide based on the technology licensed from Zengen. The technology involves a treatment system using one or more polypeptides for treatment of uro-genital conditions. Uro-genital conditions can include infections, inflammation or both. The Directors confirm that the protection period of the aforementioned technology patented or pending to be patented by the United States Patent and Trademark Office to Zengen was 20 years from the date of grant.

Currently, the Group has the following new products under research and development by the Group's research and development department:

Product name	**Generic name**	**Medical category**	**Dosage form**	**Medical application**	**Development stage**	**Technology used**
Declotana	Anti-platelet thrombolysin enzyme	Category 1 biopharmaceutical product	Lyophilized powder for injection	Treatment for unstable angina (不穩定心絞痛), myocardial infarction and stroke	Application for clinical trial submitted to the SDA	Snake venom
Protein-free calf blood extract eye gelatin	Calf serum extract	Category 4 biopharmaceutical product	Topical gel	Treatment for cornea ulcer	Application for clinical trial submitted to the SDA	Water-based gel delivery
Livaracine for new indication *(note)*	Low molecular weight heparine calcium	Category 5 biopharmaceutical product	Lyophilized powder for injection	Treatment of kidney diseases	Application for clinical trial submitted to the SDA	Low molecular weight heparin
Hemocoagulase	Factor X activator	Category 4 biopharmaceutical product	Lyophilized powder for injection	Treatment for internal bleeding such as gastric ulcer (胃潰瘍), bleeding caused by trauma (創傷), bleeding caused by surgery	Pre-clinical study commenced	Snake venom

Product name	Generic name	Medical category	Dosage form	Medical application	Development stage	Technology used
Anti-fugus peptide	Tri-peptide	Category 1 biopharmaceutical product	Topical gel	Treatment of yeast infection vaginitis	Pre-clinical study commenced (representing a licensed technology from Zengen)	Water-based gel delivery
Livaracine *(note)*	Low molecular weight heparin calcium	Category 4 biopharmaceutical product	Topical gel	Skin disease	Pre-clinical study commenced	Water-based gel delivery
Livaracine *(note)*	Low molecular weight heparin calcium	Category 4 biopharmaceutical product	Oral	Treatment for diseases associated with hyper-coagulation state	Pre-clinical study commenced	Low molecular weight heparin
Heparanase inhibitor	Heparanase inhibitor	Category 1 biopharmaceutical product	Oral or lyophilized powder for injection	Treatment for solid tumours and auto-immune diseases	Pre-clinical study commenced	Other technology

Note: Although the three products are Livarcine (low molecular weight heparin calcium) in nature, it is the policy of SDA to require separate applications for three different New Medicine Certificates for each of the products existing in different dosage forms/with different medical indications.

PRICING POLICY

At present, ZHAOKE Defibrase, ZHAOKE Livaracine and ZHAOKE Yallaferon which are produced by the Group, are subject to price control in the PRC. For each of the three years ended 31st December, 2001, sales of the products which were subject to the price control by the State represented 100.0 per cent., 100.0 per cent. and 100.0 per cent., respectively, of the Group's turnover. Despite the price control on certain of the Group's products, for each of the three years ended 31st December, 2001, the Group still achieved a gross profit margin for its manufacturing business of approximately 61.2 per cent., 71.7 per cent. and 76.2 per cent., respectively. During the Track Record Period, the Group has made an application for price adjustments for one of the Group's products. Applications of the Group's pharmaceutical products for future price adjustments to the relevant price control administrative authorities would be made on an individual basis. The Directors believe that such applications, if made on reasonable grounds, would not be denied.

INTELLECTUAL PROPERTY RIGHTS

The Group's products are all sold under the trademark of "ZHAOKE", which has been registered in the PRC since 1996. The trademark is not registered outside the PRC.

Based on the snake venom technology as set out in the paragraph headed "Research and development" in the section headed "Business" to this prospectus, the Group has filed a patent application with the United States Patent and Trademark Office in April 1998 for Declotana, a Category 1 new drug of the Group. As at the Latest Practicable Date, the Group has completed the claims notification procedure and most of the claims have been allowed. The Directors

expect that the application for the patent can be approved in late 2002. The Directors consider that the obtaining of the patent for Declotana will enhance the Group's market recognition both in the PRC and in the United States, and will boost the sale of the Group's existing products and new products in the marketplace.

Based on the water-based gel delivery technology as set out in the paragraph headed "Research and development" in the section headed "Business" to this prospectus, the Group has also filed patent applications for its proprietary formulation for topical delivery of interferon as well as its production process with the IPB in July 1997. In addition, based on the snake venom technology as set out in the paragraph headed "Research and development" in the section headed "Business" to this prospectus, a patent application conveying the manufacturing process of Declotana was filed with IPB in February 2001. The patent applications with IPB are currently under review.

The Group's licensed peptide technology from Zengen covered by a total of 2 patents relating to uro-gential condition treatment pending-to-be-issued by relevant authorities in the United States with a protection period of 20 years from the date of grant.

INSURANCE

The Group maintains insurance policies which cover its fixed assets and against loss and damage caused by accidents and natural disasters (including fire hazards and explosions). The Group also makes contributions to the retirement and unemployment benefits insurance schemes for its employees in the PRC. Furthermore, the Group has also taken out insurance to cover loss arising from business interruption caused by natural disasters. In accordance with the established practice in the PRC, however, the insurance policies maintained by the Group do not cover any indirect losses (such as loss of profits) caused by cessation of its business. Other than motor vehicle insurance, the Group has not taken out any third party liability insurance in the PRC to cover any claims relating to any personal injury or any deterioration of pharmaceutical products sold by the Group. The Group has not purchased any product liability insurance which is not mandatory under the prevailing laws of the PRC. The Group also maintains a medical insurance plan for employees in Hong Kong. Since its commencement on production, the Group has not experienced any material third party liability claim in relation to its products. The Directors believe that the Group can effectively control the product liability risks through stringent control of its operations and products. Moreover, the Group has to meet various standards and requirements imposed by the regulatory authorities in the PRC in order to obtain and maintain the required certificates, permits and approvals for the production, sale and distribution of its pharmaceutical products from time to time.

FOREIGN EXCHANGE

Currently, all of the revenues generated from the sales of pharmaceutical products by the Group are in Renminbi. The Directors believe that subject to the risk factors set out in the paragraphs headed "Currency risk" and "Currency conversion and foreign exchange control" in the section headed "Risk factors" of this prospectus, the Group does not have foreign exchange problems in meeting its foreign exchange requirements. The Group has not used any type of derivatives to hedge against any foreign currency fluctuations.

ENVIRONMENTAL ISSUES

The Directors believe that the current production of the Group at Zhaoke, which is GMP-compliant, does not generate any environmental-unfriendly by-products which are subject to environmental regulations of the PRC. Since its establishment, the Group has not been prosecuted or penalised for the breach of any national, provincial or local environmental protection law or regulations promulgated by the State, provincial or local governments in the PRC.

COMPETITION

According to the 深圳證券信息有限公司 (Shenzhen Securities Information Company Limited), there are over 6,700 manufacturers in the PRC producing pharmaceutical products. While the market is in keen competition in terms of the number of participants in the industry, the production and research capacities of pharmaceutical manufacturers vary. Pursuant to the "關於實施《藥品生產質量管理規範》有關規定的通知" (Notice regarding the Implementation of Good Manufacturing Practice) in 1999, the SDA has made it mandatory that all manufacturers of lyophilized powder for injection and bulk pharmaceutical for injection who do not have GMP certification will be prohibited from producing those dosage forms starting from 1st January, 2001. In 2001, SDA issued "關於全面加快監督實施藥品GMP工作進程的通知" (Notice on the Overall Acceleration of the Implementation and Supervision of Good Manufacturing Practice for Pharmaceutical Products), in which SDA requires all pharmaceutical manufacturing enterprises to comply with the GMP Standards by 30th June, 2004. The Directors believe that the Group's GMP compliant pharmaceutical manufacturing plant in Hefei, Anhui Province, the PRC places the Group in an advantageous position in view of the fact that there are currently, only 352 out of 450 lyophilized powder for injection manufacturers and a total of less than five gel manufacturers that are GMP compliant according to information from the SDA as at 26th July, 2001. The Directors consider that pharmaceutical manufacturers in the PRC that are not GMP compliant will not be able to compete effectively with the Group in the long run.

As far as the Group's existing three pharmaceutical products are concerned, there are at present manufacturers producing similar type of products in the PRC or from overseas manufacturers. Specific instances of competition are analysed as follows:

Competition against Yallaferon from injection form interferon

At present, there are several pharmaceutical manufacturers in the PRC producing injection form interferon which are for the treatment of Hepatitis B and other viral infection diseases such as genital warts.

The Directors believe that the Group is in a position to capture the market shares of genital warts market in the PRC as Yallaferon is the first of its kind produced in topical gel form in the PRC market which is easier to apply and has better efficacy with fewer side effects over its injection form counterparts. As advised by the Directors, it is impossible to assess the Group's market share in the PRC at this stage as the product is newly launched and is the only available product in its category.

Competition against Livaracine from overseas and local manufacturers

At present, there is one overseas pharmaceutical manufacturer in France producing low molecular weight heparin calcium which is currently being sold in the PRC and to the best knowledge of the Directors, such product is currently the market leader. The Directors believe that the Group is able to compete effectively with this overseas manufacturer as the Group's Livaracine is of similar efficacy with a competitive price. As further advised by the Directors, there is one local manufacturer producing low molecular weight heparin calcium. The low molecular weight heparin calcium from this manufacturer is of different dosage form. The Directors believe that the Group's Livaracine can compete with this manufacturer effectively as the Group's Livaracine is in lyophilized powder which is easier to use and store. The Directors estimate that the market share for the Group's Livaracine is approximately 7 per cent. at present.

Competition against Defibrase from local pharmaceutical manufacturers in the PRC

In the PRC, there are currently 48 pharmaceutical manufacturers approved by the SDA to produce Defibrase under respective brandnames. All of the Defibrase manufactured by various manufacturers are under the same specifications with the same indication and of the same selling price within the PRC. The Directors estimate that the Group has captured approximately 3 per cent. market share in the PRC at present.

Although keen competition exists in the products manufactured by the Group, the Directors believe that in view of the recognised quality of its products, the economies of scale achieved by its production workshops and its extensive marketing network, the Group can compete effectively with its competitors.