HUTCHISON CHINA MEDITECH LIMITED
和黃中國醫藥科技有限公司

# 2008 Annual Report


China Healthcare


Drug Research & Development


Consumer Products

A Hutchison Whampoa Company

# Corporate Information

## BOARD OF DIRECTORS

### Executive Chairman
Simon TO, BSc, ACGI, MBA

### Executive Director
Christian HOGG, BSc, MBA
*Chief Executive Officer*

### Non-executive Directors
Shigeru ENDO, BA
Christian SALBAING, BA, LLL, JD
Edith SHIH, BSE, MA, MA, EdM, Solicitor, FCIS, FCS (PE)

### Independent Non-executive Directors
Christopher NASH, BSc, MBA, ACGI
*Senior Independent Director*
Michael HOWELL, MA, MBA, HonFCGI
Christopher HUANG, BA, BMBCh, PhD, DM, DSc

## AUDIT COMMITTEE
Michael HOWELL (Chairman)
Christopher HUANG
Christopher NASH

## REMUNERATION COMMITTEE
Simon TO (Chairman)
Michael HOWELL
Christopher NASH

## TECHNICAL COMMITTEE
Christopher HUANG (Chairman)
Simon TO
Christian HOGG

## COMPLAINTS COMMITTEE
Simon TO
Christian HOGG
Michael HOWELL
Edith SHIH

## COMPANY SECRETARY
Edith SHIH

## NOMINATED ADVISER
Lazard & Co., Limited

## CORPORATE BROKERS
Investec Bank plc
Panmure Gordon (Broking) Limited

## AUDITOR
PricewaterhouseCoopers

# Contents

# Our Business

Chi-Med's aim is to become the leading player in the development of modern, science-based pharmaceutical and consumer products derived from traditional Chinese medicine ("TCM") to serve both the Chinese and the global healthcare markets

China Healthcare

Drug Research and Development

Consumer Products

## China Healthcare

We have three operating joint ventures in the fast growing China TCM market. These joint ventures are increasingly strong cash generators from the development, manufacture and marketing of both prescription and over-the-counter TCM pharmaceuticals and health supplements. We plan to establish further joint ventures in the future.

## Drug Research and Development

Through Hutchison MediPharma Limited, Chi-Med researches and develops TCM-derived botanical, semi-synthetic natural product drugs and small molecule drugs for the global market. We focus on the oncology and auto-immune therapeutic areas.

## Consumer Products

Chi-Med is developing Sen as a quality TCM consumer brand in TCM medicines and treatments, food & beverage, and skin and body care products through its own network of retail stores and third party luxury goods retailers.

# Highlights

## Group Results

- Sales up 34% to $87.0 million (2007: $65.1 million). Growth across all divisions. Particularly strong organic growth in the China Healthcare division.
- Operating loss reduced to $14.2 million (2007: -$14.8 million) reflecting profit growth in China Healthcare offset by higher research and development and consumer products investment.
- Net loss attributable to equity holders of Chi-Med of $17.8 million (2007: -$17.2 million).

## China Healthcare Division

- Sales up 31% to $80.7 million (2007: $61.4 million). Operating profit up 34% to $9.1 million (2007: $6.8 million).
- Net profit after tax attributable to equity holders of Chi-Med up 30% to $5.9 million (2007: $4.5 million).
- Due diligence continues on potential acquisitions and joint ventures.

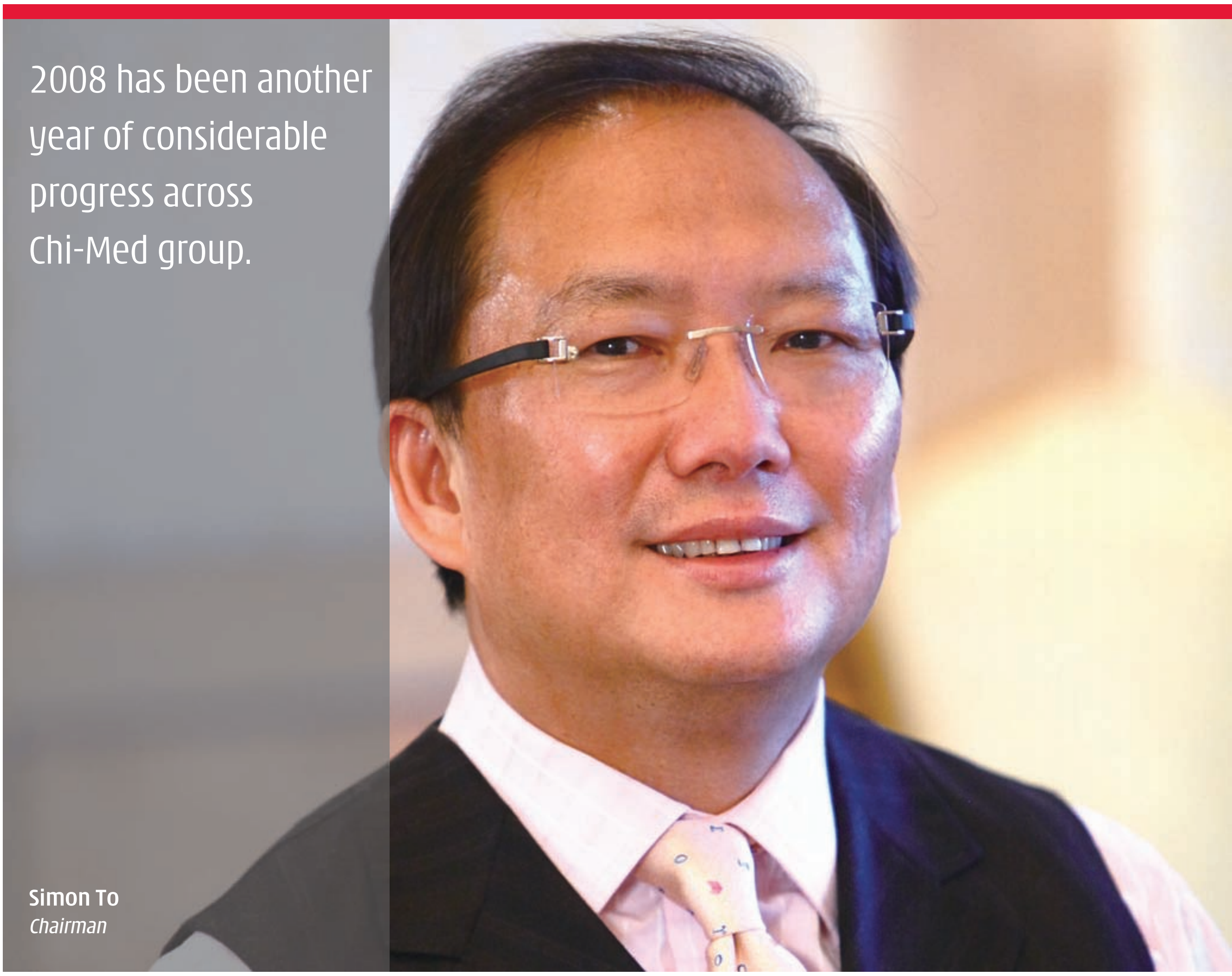
## Drug R&D Division

- Sales up 156% to $2.3 million (2007: $0.9 million) from strategic partnership income.
- Operating loss of $15.4 million (2007: -$10.1 million) reflecting planned investment.
- Expansion of strategic partnership in oncology with Eli Lilly and Company.
- New strategic partnership in inflammation with Ortho-McNeil-Janssen Pharmaceuticals, Inc.
- Group's lead drug candidate HMPL-004 with US Phase II Crohn's disease trial to report in mid-2009.
- Three novel small molecule compounds in late preclinical development. 66 global patent applications filed by the end of 2008.

## Consumer Products Division

- Sen sales up 41% to $4.1 million (2007: $2.9 million). 17% like-for-like sales growth in existing London shops.
- Distribution in 125 Marionnaud shops in France and three new London shops opened.

# Chairman's Statement



2008 has been another year of considerable progress across Chi-Med group.

**Simon To**
*Chairman*

2008 has been another year of considerable progress across the Chi-Med group (the "Group"). Group sales grew 34% to $87.0 million (2007: $65.1 million), primarily reflecting the strong China Healthcare Division, while the net loss attributable to Chi-Med shareholders widened slightly to $17.8 million (2007: -$17.2 million), this reflected the planned increase in investment in our Drug Research and Development business and consumer products expansion.

## STRATEGIC OVERVIEW

Our overall strategy for Chi-Med remains the same as in previous years. We apply modern science and business practice to TCM, in order to realise the substantial potential of novel TCM-based products, both for the China and the global pharmaceutical and consumer products markets. Chi-Med's goal continues to be the building of a unique and well-balanced portfolio of businesses that enables us to manage both the pace of growth and the risks associated with it.

China Healthcare Division – We continue to see particularly strong opportunity in the China healthcare market, not least because it is supported by the Chinese Government's healthcare policy. With our range of fast growing and profitable products, we continue to target organic growth of about 20% a year for the foreseeable future.

Our China Healthcare strategy is to combine organic growth with selective acquisitions and joint ventures. We have a strong track record of value creation on our China healthcare acquisitions to date. An example of this is our joint venture, Hutchison Whampoa Guangzhou Baiyunshan Chinese Medicine Company Limited ("HBYS"), which since its establishment in early 2005 is expected in 2009 to achieve full pay back of our initial $15.1 million cash investment, through dividends and shareholder loan repayments. We continue to benefit from the infrastructure, reputation, experience and depth of connections of Hutchison Whampoa in China to identify and evaluate potential value-creating acquisitions and joint ventures.

*Drug R&D Division* – TCM, with its botanical origins, has a history that is centuries old and has demonstrated its efficacy and safety under modern scientific scrutiny over several decades. We see it as a major and substantially untapped reservoir of novel drugs for the global pharmaceutical market. Our Drug R&D Division is dedicated to using the highest standards of modern science to identify and develop both botanical substances and small molecule compounds derived from TCM, which can deliver new treatments, especially in the areas of oncology and auto-immune diseases.

In 2008 we established a new holding company structure and an employee share option scheme primarily for the Hutchison MediPharma group, Chi-Med's wholly owned Drug R&D Division. The purpose of this move was to align better the interests of our team of pharmaceutical executives and scientists with the interests of Chi-Med shareholders. The recognised quality of our Drug R&D business is reflected both by the range of strategic partnerships we engage in, on which we earn upfront and/or maintenance payments as well as success-based milestone payments; and the progress of our own novel drug candidates in the oncology and auto-immune areas. Last year we expanded our relationship with Eli Lilly and Company ("Eli Lilly") and signed a new partnership in inflammation with Ortho-McNeil-Janssen Pharmaceuticals, Inc. ("J&J"), part of the Johnson & Johnson family of companies. All these give us great confidence that we have a best-in-class operation with significant potential, and we await our important US Phase II Crohn's disease trial results with HMPL-004 in the middle of this year.

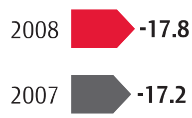
*Consumer Products Division* – The Sen group of companies located in the United Kingdom ("UK"), France and Hong Kong (collectively "Sen") delivered impressive like-for-like sales growth and, during 2008, we took action on the second strand of its strategy – building third party distribution. We leveraged synergy with Hutchison Whampoa's global chain of over 8,300 health and beauty shops, of which over 1,600 are prestige/luxury focused and consistent with Sen's brand image. We launched a range of Sen products through an initial 125 Marionnaud shops in France and the initial results are encouraging.

# +34%

*Organic sales growth of existing operations*

## Sales* (US$ million)


## Net Loss Attributable to Equity Holders (US$ million)




* on continuing operations

# Chairman's Statement

## CORPORATE GOVERNANCE

We maintain high standards of corporate governance to build the long-term interests of the Company and maximise the long-term returns to shareholders.

During 2008 the Chi-Med Board remained largely unchanged apart from the departure of Mr Patrick Wan and the appointment of Mr Shigeru Endo. I would like to take this opportunity to thank Mr Wan for his involvement over the past years and wish him well in his continued career within the Hutchison Whampoa Group. We are very pleased to have Mr Shigeru Endo, Chief Executive Officer of Hutchison Whampoa Japan K.K. join us as a Non-executive Director. As a group, our Independent Non-executive Directors bring a wealth of expertise on AIM and growth businesses, corporate governance, and pharmaceutical research and development. They have and continue to make a valuable contribution to the evolution of Chi-Med and I very much appreciate their involvement and wish to thank them all for their efforts.

## DIVIDEND

The Board has decided not to recommend a dividend for the year ended 31 December 2008.

Over the coming years, Chi-Med will continue making significant investments in its businesses, in which we see substantial opportunity to enhance shareholder value.

The substantial progress that Chi-Med has made is the result of the quality and commitment of our strong management team and all our employees and partners. My thanks and deep appreciation goes to them all.

**Simon To**
Chairman

13 March 2009

# Chief Executive Officer's Statement

The Group performed as expected in 2008 with overall sales up 34% to $87.0 million.

**Christian Hogg**
*Chief Executive Officer*

## GROUP RESULTS

The Group performed as expected in 2008 with overall sales up 34% to $87.0 million. This reflected continued strong organic growth in our China Healthcare Division where sales grew 31% to $80.7 million; a step-up in revenues to $2.3 million in our Drug R&D Division, from its strategic collaborations; and a 41% increase in Sen's sales, our Consumer Products Division.

The China Healthcare operating profit increased 34% to $9.1 million (2007: $6.8 million). Each of its three operating companies is well established and performing ahead of the general China market thanks to quality management, established brands and products, and increasing operational scale and distribution. Coupled with the Chinese Government's recent healthcare reforms, our China Healthcare Division has the ability to sustain substantial profitable growth and build its position as an important player in the overall China healthcare market.

# Chief Executive Officer's Statement

Our Drug R&D business, Hutchison MediPharma Limited ("HMPL"), also made further good progress. Its lead drug candidate, HMPL-004, awaits Phase II trial results in the middle of this year, and it has added two novel small molecule compounds in late pre-clinical development. It has also built on its strategic partnerships, which balance financial risk in discovery and development stages, generate increasing third-party income streams and augment our in-house know-how. During 2008 we expanded our collaborations with Eli Lilly and formed a new partnership with J&J, as well as continuing to build our relationship with Merck Serono (previously known as Merck KGaA) ("Merck"). 2008 was, as planned, the peak cash burn for HMPL in its development; and despite its revenue growth, its operating loss widened from $10.1 million to $15.4 million.

Investment continues in the expansion of Sen albeit on a relatively small scale. In the UK, it grew like-for-like sales by 17% and, despite three new shop openings, narrowed its operating loss to $1.8 million (2007: -$2.1 million). Sen also expanded into France, incurring start-up costs of $0.8 million (2007: Nil), so that its overall operating loss widened to $2.6 million (2007: -$2.1 million).

Group overhead costs were $5.4 million (2007: $4.3 million) reflecting the tight cost control with the head office management team and operations; legal, professional, and management services fees associated with being a listed company; and due diligence fees on potential acquisition and joint venture projects.

The Group's overall operating loss was $14.2 million, compared to $14.8 million in 2007.

Our tax charge was $1.5 million (2007: $0.8 million) reflecting the growth in China Healthcare profitability, but benefiting from the low corporate income tax rates of 12.5% on both HBYS and Shanghai Hutchison Pharmaceuticals Limited ("SHPL"). These rates which are approximately 50% of normal China enterprise income tax rates are the result of tax holidays granted at the start of these joint ventures. These holidays are set to expire in 2009; but both SHPL and HBYS have recently been granted the High and New Technology Enterprise status. As such, they will receive preferential tax status until the end of 2010, with an enterprise income tax rate of 15%. It is expected that our China Healthcare Division's corporate tax expense will be reduced by about $0.7 million in 2010. The High and New Technology Enterprise status is renewable beyond 2010 subject to reapplication and approval. In addition to enterprise income tax in China, we now pay 5% withholding tax on dividends derived from post 2007 earnings remitted outside China, the accrual for such item totalled $0.3 million (2007: Nil).

Finance costs of $0.5 million (2007: $0.3 million) were incurred primarily as a result of borrowing in SHPL and Hutchison Healthcare Limited ("HHL"). However, the Group remains relatively un-leveraged with a gearing ratio of only 10.1% (2007: 7.3%).

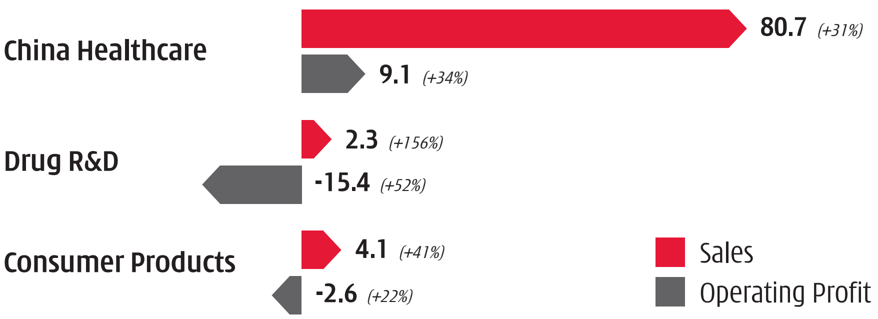
Profit attributable to minority interests increased to $1.5 million (2007: $1.2 million) as HBYS continued to improve performance significantly.

In total, the Group's net loss attributable to equity holders increased slightly to $17.8 million from $17.2 million in 2007.

The Group maintains a strong balance sheet and ended the year with net assets of $84.4 million, including cash and cash equivalents totalling $38.2 million (2007: $53.3 million). The Group has no debt outside of the China Healthcare Division. As at the end of 2008, the China Healthcare Division held bank loans totalling $7.6 million or 0.8 times 2008 EBITDA. The strong cash position and low levels of debt put Chi-Med in a good position to continue aggressive execution of strategies in our three core Divisions.

## 2008 Performance by Division

US$ million (% change 2008 vs. 2007)



# China Healthcare


## Market Overview

We continue to believe that the China healthcare market, and particularly the TCM segment, will grow strongly and our China Healthcare Division remains well positioned to deliver sustained and profitable growth. The Chinese Government's healthcare policy and reform, drug reimbursement system and position on TCM all appear to benefit the Group's operations.

## Chinese Government Healthcare Policy and Reform

In January 2009, the China State Council approved in principle the final draft of its healthcare reform programme which laid out Government spending of RMB 850 billion ($124.3 billion) over the next three years, with an objective of providing accessible and affordable healthcare to the country's 1.3 billion population.

China's Basic Medical Insurance System ("BMIS") is a nationwide system, which currently includes four schemes, the basic medical insurance schemes for urban employees; urban residents in general targeting primarily the unemployed; the rural cooperative medical insurance scheme; and medical aid for the poor in both rural and urban areas. According to the National Bureau of Statistics of China, approximately 223 million people were enrolled in the basic medical insurance schemes for urban employees and urban residents as at the

# China Healthcare

Sheng Nong TCM Garden – HBYS


Banlangen – HBYS

end of 2007 (2006: approximately 160 million). We believe that this 39% growth in enrolment is an important driver behind the China healthcare industry growth of approximately 20% per annum.

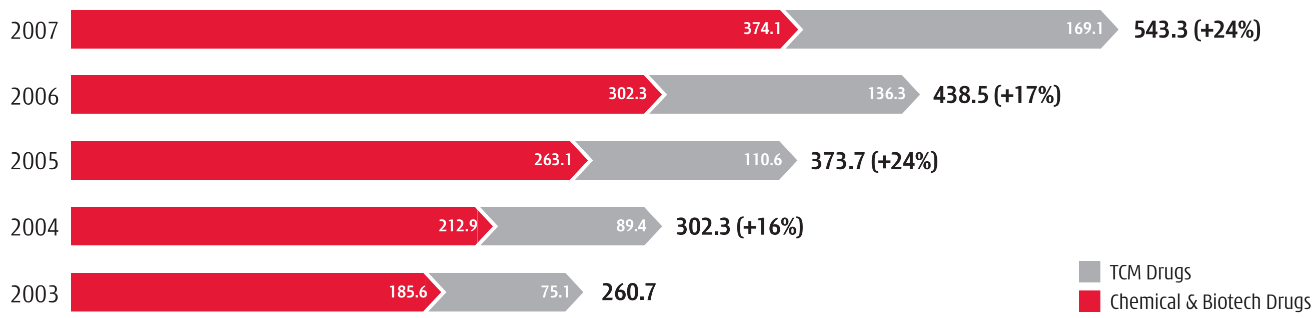
Under the reform, the Chinese Government plans to broaden basic medical insurance coverage of both rural and urban population to at least 90% of the population by 2011. It is expected that each person covered by the basic medical insurance scheme for urban residents and the new rural cooperative medical insurance scheme would receive an annual subsidy of RMB 120 to help pay healthcare costs.

In order to make healthcare more accessible to rural communities, the Chinese Government will start investing in 2009 to overhaul the rural medical care infrastructure that will provide services. As reported by China Daily in January 2009, the Minister of Health said that the central budget will allow for the building of about 2,000 county-level hospitals in the next three years with the goal to ensure that each of China's 1,600 counties has at least one hospital of a national standard.

## Regulatory/Reimbursement Framework

Currently the authorities regularly review all drugs in China and regulate reimbursement by assigning each drug a classification on the National Medicine Catalogue ("NMC") and Provincial Medicine Catalogues ("PMC"). Drugs most commonly included on the NMC and PMC, and thereby reimbursed, are those that are necessary clinical treatments, which have wide application, good effect, and are low cost. Under the healthcare reforms, starting from 2009, the Chinese Government will also build a basic medicine system that includes a catalogue, the Basic Medicine Catalogue ("BMC"), of necessary drugs produced and distributed under its control and supervision. The BMC is expected to reduce the number of reimbursed drugs from over 2,000 (773 western medicine and 1,260 TCM were included in the 2004 version) to about 300, according to a PiperJaffray analyst report on China heathcare of January 2009. Chi-Med's core products are all either on the NMC or PMC and we remain confident that this will continue under the new BMC system.

## China Pharmaceutical Sales (ex-factory) (RMB billion)




*Source: State Information Center, Department of Economic Forecasts*
*Note: RMB 6.9027: US$1.00 (Rate as at December 2008)*

With the expansion of the BMIS, we believe that the demand for drugs on the BMC will increase significantly. In addition, the competition to gain access to the BMC should also increase. The Group is very well placed in this new environment as our over-the-counter ("OTC") products have the high scale and low cost of production needed to ensure we are competitive in generic BMC drug tenders. Our main prescription drugs are proprietary and therefore not subject to tender.

### Chinese Government position on TCM

As in the past several years, the Chinese Government continued to encourage the development and use of TCM throughout 2008. Latest Chinese Government data (up to 2007) again shows continued strong performance of the TCM drug industry relative to the chemical and biotech drug industry. Based on data published by Chinagate.com.cn in April 2008, TCM grew by 24.1% to RMB 169.1 billion ($22.3 billion) in 2007 (2006: RMB 136.3 billion), once again slightly ahead of the chemical and biotech drug industry, which grew 23.8% to RMB 374.1 billion ($49.4 billion) in 2007 (2006: RMB 302.3 billion).

TCM is a highly sophisticated and developed sector in China that is a generally lower cost and effective means of healthcare. As the Chinese Government seeks to expand state-funded healthcare coverage across China, we believe that it will continue to support TCM as it is clearly in its best interests to do so.

### China Healthcare Division performance

Chi-Med's China Healthcare Division sales grew 31% to $80.7 million (2007: $61.4 million) and operating profit grew 34% to $9.1 million (2007: $6.8 million). Net profit after tax attributable to Chi-Med equity holders grew 30% to $5.9 million (2007: $4.5 million).

Since our IPO in mid-2006, our China Healthcare Division has blossomed with compound annual growth in sales of 29%, from $37.2 million in 2005 to $80.7 million last year, and operating profit increasing over 15 times from $0.6 million in 2005 to $9.1 million in 2008.

# China Healthcare

## China Healthcare Division

### Sales (US$ million)

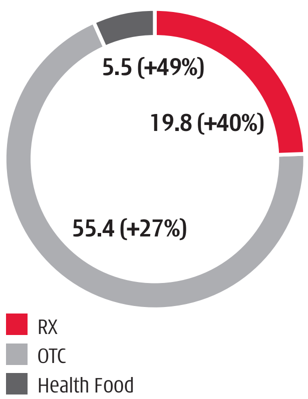

### Operating Profit (US$ million)


### Net Profit After Tax Attributable to Equity Holders

(US$ million)


### Sales by Sub-sector

US$ million (% change 2008 vs. 2007)




Chi-Med's China Healthcare Division now employs a total of over 3,700 staff, about 1,200 of these in two large-scale factories in Guangzhou and Shanghai and about 2,300 in sales, marketing, and distribution operations in over 200 cities in China, up from 1,800 in 2007.

To illustrate the scale of our operations in China, Chi-Med manufactured and sold over 4 billion doses of medicine last year and combined domestic sales by HBYS, SHPL and HHL in 2008 were $155.8 million (2007: $123.6 million) of which Chi-Med, under the accounting principles of the International Financial Reporting Standards, consolidates 50% of the two jointly controlled entities (HBYS and SHPL) and 100% of HHL domestic sales. Our product portfolio is well diversified with 91% of the Group's China Healthcare Division sales in 2008 coming from eight core products of which four are OTC; three prescription; and one health food.

### OTC Drugs

OTC drug sales through HBYS increased 27% in 2008 to $55.4 million (2007: $43.6 million), all of which was organic growth. Since HBYS was formed in mid-2005 compound annual sales growth has averaged 31%, which we believe, makes HBYS one of the fastest growing, large-scale OTC drug businesses in China.

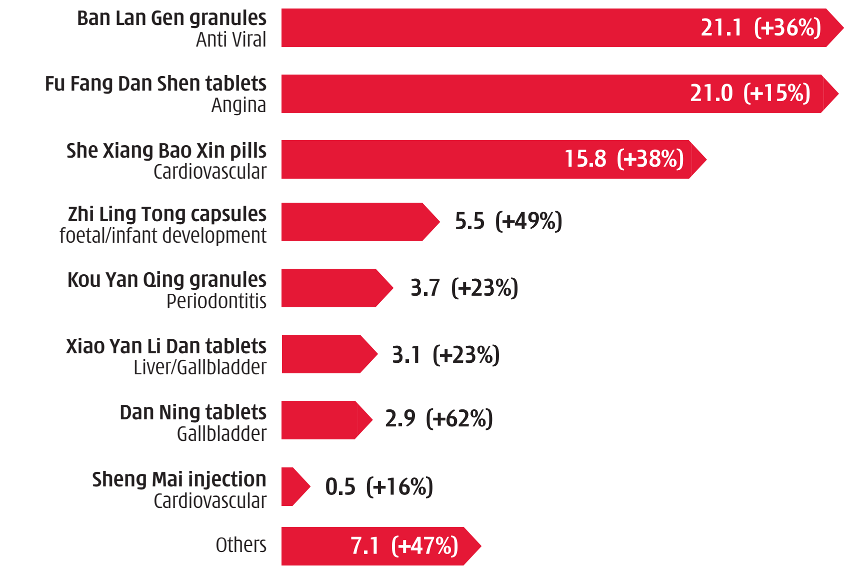
HBYS's OTC distribution network grew significantly in 2008 and now has about 1,500 sales and marketing staff up from 1,200 in 2007, covering all cities with a population over 1 million. These staff co-operate with the over 280 local distributors in all provinces of China and manage local retail activities and marketing programmes. On a regional level, HBYS made major progress in the lucrative and previously relatively un-covered east China market, as well as in north-central China. Sales in these regions grew 31% to $7.2 million (2007: $5.5 million) and 28% to $14.2 million (2007: $11.1 million) respectively. Outside these two above average markets, HBYS growth in 2008 was spread evenly across China.

As in recent years, the five major HBYS products dominated sales, accounted for 90% of total HBYS sales (2007: 92%). The fastest growing of these products were the anti-virals, Banlangen granules which grew 29% to $17.7 million (2007: $13.5 million) and Fu Fang Banlangen granules which grew 67% to $3.4 million (2007: $2.0 million). HBYS's largest product Fu Fang Dan Shen tablets for angina had another strong year with sales growth of 15% to $21.0 million (2007: $18.2 million). Beyond the top five products progress was made on the Baiyunshan brand herbal drink which grew 92% to $1.2 million (2007: $0.6 million).

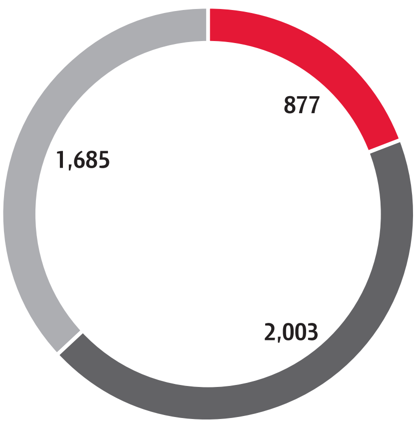
In 2008, HBYS overcame challenges posed by increasing raw material and labour costs by instituting an aggressive cost control programme. An increase in product and intermediate material outsource production along with the effective establishment of Enterprise Resource Planning systems and procedures enabled HBYS to keep gross margins flat at 54.2% (2007: 54.4%).

## China Healthcare Division Product Portfolio 2008 Sales

US$ million (% change 2008 vs. 2007)




**Total $80.7m**



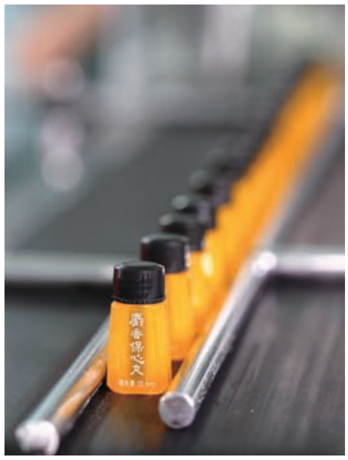

## Number of Manufacturers in China Pharmaceutical Industry 2007

- TCM Drugs Manufacturers
- Chemical & Biotech Drugs Manufacturers
- TCM, Chemical & Biotech Drugs Manufacturers

*Source: State Food & Drug Administration Southern Medical Economics Research Institute*


Ban Lan Gen granules


Fu Fang Dan Shen tablets

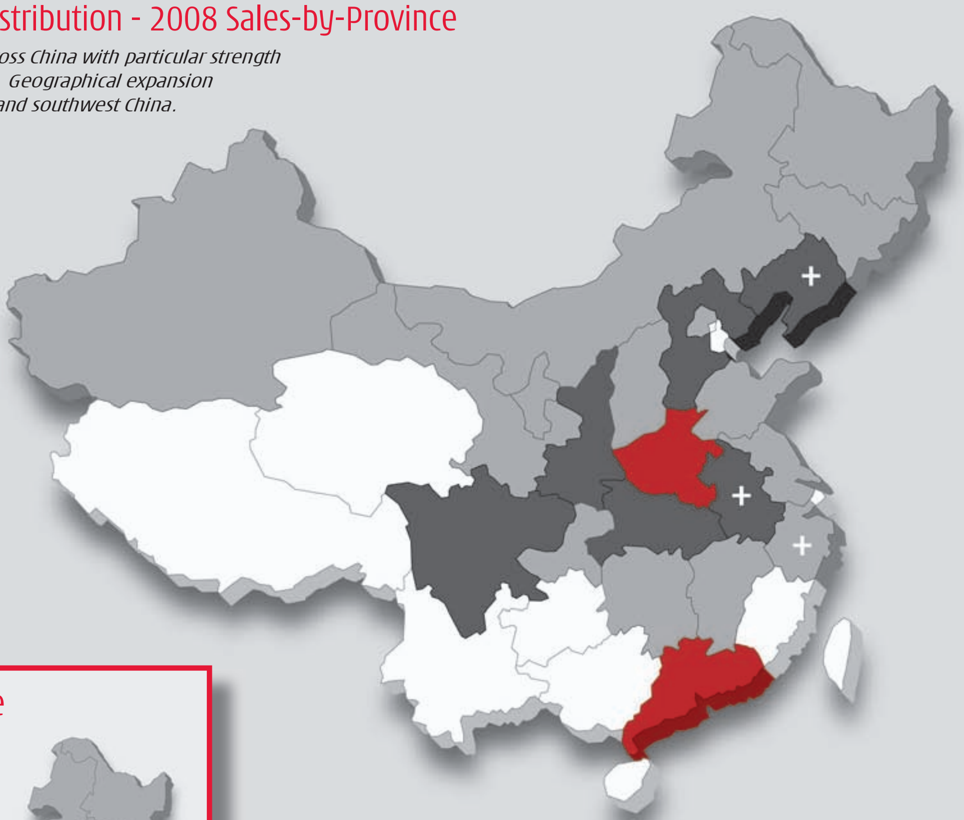


She Xiang Bao Xin pills

# China Healthcare

## HBYS China Sales Distribution - 2008 Sales-by-Province

*HBYS continues to expand across China with particular strength in central and southern China. Geographical expansion potential lies in both eastern and southwest China.*



"+" Provinces that stepped-up to higher sales level in 2008.

## 2007 Sales-by-Province

**Sales Level**

- > US$10.0 million Net Sales
- US$5.0 - 10.0 million Net Sales
- US$1.0 - 4.9 million Net Sales
- < US$1.0 million Net Sales

As an OTC pharmaceuticals business, our core focus is on building awareness, credibility, and loyalty towards our Baiyunshan (meaning "white cloud mountain") brand. HBYS constantly strives to promote an image of social responsibility for the brand through community activities. In 2008, these included: expansion of the expired medicine exchange programme to many Chinese cities where consumers can bring expired medicine and exchange it for new Baiyunshan products for free; publishing the first "Social responsibility report for the China pharmaceutical industry"; being one of the first pharmaceutical companies to aid the Sichuan earthquake victims by providing cash, free medicine, and disease prevention programmes; coordinating


the "Chengdu Announcement" together with Alzheimer's prevention associations, professionals, scholars and the local government to raise awareness of Alzheimer's disease; and, opening the Sheng Nong TCM garden in HBYS to the public for free.

These activities received broad scale media coverage on a national and regional level which, combined with conventional marketing activities, have continued to help build Baiyunshan brand market share and loyalty.

In research and development, HBYS made major progress in 2008 with a total of 14 projects receiving commitments for financial support totalling more than RMB 9 million from China State, Provincial, and local governments. These projects include research on new TCM technology platforms, research and development on new TCM drugs and therapeutic areas, and construction of new Good Agricultural Practice sites in China. This year, HBYS was granted 17 patents by the China State Patent Bureau, and a further 7 submissions were made. The broad ranging technical innovation at HBYS was one of the factors helping it achieve High and New Technology Enterprise designation.

By the end of 2008, based on technical merit and competitive production costs, a total of 62 HBYS products were included in the NMC representing approximately 7.5% of the total 823 TCM product NMC reimbursement listings in China. HBYS also achieved strong results in open bidding to gain inclusion of products on various PMCs in order to receive reimbursement on a provincial level, with particular progress being made in Henan and Guangdong provinces.

## Prescription Drugs

Prescription drug sales through SHPL grew 40% to \$19.8 million in 2008 (2007: \$14.1 million) all of which was organic from existing products. Since the establishment of SHPL in 2002 compound annual sales growth has averaged 19%, with particularly strong growth in the past two years now that SHPL's commercial operations are well established.

SHPL increased sales of its key cardiovascular prescription drug She Xiang Bao Xin pill ("SXBXP") by 38% to \$15.8 million (2007: \$11.5 million). In 2008, we focused on this product and have built very strong momentum behind it, which we expect to carry over into 2009. Encouragingly, we saw fast growth of our second product Dan Ning tablet (gallbladder) in which sales grew 62% to \$2.9 million (2007: \$1.8 million). Dan Ning's growth was spurred by the grant of a 20-year process and formula patent from the State Patent Bureau in mid-2007 and as a result allowed us to attain NMC inclusion and reimbursement status.

Regionally, SHPL continued to make progress in expanding beyond our historical Shanghai stronghold, which in 2008 represented 33% of sales (2007: 46% and 2006: 48%). Sales in markets outside Shanghai grew 70% during 2008 to \$13.2 million (2007: \$7.7 million). Importantly, a continued encouraging sign for SHPL in 2008 was that in-market consumption grew 56%, outpacing ex-factory sales growth of 40%, and signifying that distributor, hospital pharmacy and chain drugstore inventories were again reduced during the year, as they were in 2007. Sales in the hospital pharmacy channel as a percentage of total SHPL sales expanded to 74% (2007: 72%) and grew 60% versus 2007, which outpaced chain drugstore channel growth of 55%. This is to be expected as SHPL generally enters new markets through hospital pharmacy distribution and once the market is established, it will expand into surrounding chain drugstores.

# China Healthcare

*Hutchison Whampoa Guangzhou Baiyunshan Chinese Medicine Company Limited*

*Shanghai Hutchison Pharmaceuticals Limited*

Behind SHPL's strong performance were two important strategic activities. First, SHPL continued to build a powerful commercial team, which grew to over 800 sales and marketing staff by the end of 2008 (2007: approximately 600). These 800 staff are divided into four teams: Hospital Sales; Community Promotions; Commercial and Distribution Channel; and Patient Education and OTC. Tight discipline and effective organisational control, training, performance appraisal, and reward of these commercial teams have driven success. Secondly, SHPL continued to build strong China State, Provincial, and local government relationships and support. In addition it was designated a High and New Technology Enterprise and will enjoy preferential tax status.

## SHPL China Sales Distribution - 2008 Sales-by-Province

*SHPL is starting to show good progress in geographic expansion of SXBX pill beyond our relatively limited regional east-China stronghold.*

"+" Provinces that stepped-up to higher sales level in 2008.

## 2007 Sales-by-Province

**Sales Level**

- > US$10.0 million Net Sales
- US$5.0 - 10.0 million Net Sales
- US$1.0 - 4.9 million Net Sales
- < US$1.0 million Net Sales

On the production side of the business, SHPL gross margins increased to 68.2% in 2008 (2007: 64.6%) despite general inflationary pressure on production costs. Gross margins were improved as we reaped the benefits of increased volume, a full year effect of the bidding price increases we secured on SXBXP in 2007 and tightened control on all inventories and production costs.

### Health Supplements

Health supplement sales through our HHL joint venture grew 49% to $5.5 million in 2008 (2007: $3.7 million), and operating profit grew 22% to $0.3 million (2007: $0.2 million). This was the first full year of running the business after the discontinuation of

# China Healthcare

## HHL China Sales Distribution - 2008 Sales-by-Province

*Expansion opportunity for Zhi Ling Tong is significant given its relatively limited distribution today.*

"+" Provinces that stepped-up to higher sales level in 2008.

## 2007 Sales-by-Province

**Sales Level**

- > US$10.0 million Net Sales
- US$5.0 - 10.0 million Net Sales
- US$1.0 - 4.9 million Net Sales
- < US$1.0 million Net Sales

a loss making product line in late-2007. As a result of this discontinuation, we continued carrying some overheads on HHL in 2008 to manage multiple elements of the product withdrawal from market. These costs, to an extent, suppressed operating profits in 2008 but have now been almost entirely removed, opening a pathway of improved operating profit performance on HHL in 2009.

In 2008, we focused on developing our profitable Zhi Ling Tong ("ZLT") infant nutrition brand which accounted for 100% of HHL's $5.5 million in sales in 2008. In partnership with our exclusive distributor of ZLT we have successfully developed a strong

Zhi Ling Tong Infant and Toddler Nutrition

hospital and mother/baby store distribution model across China. In 2008, the number of hospitals and family planning clinics covered grew to over 400 (2007: less than 200); doctors recommending ZLT grew to over 3,100 (2007: approximately 1,100); and total mother/baby shop, drug store, and department store points of sale rose to over 3,700 (2007: approximately 2,300). Since this still represents relatively limited coverage of the China market, opportunities for ZLT and a very broad scale geographic expansion still exists.

HHL sells three ZLT licensed health food products. Sales of the largest, ZLT DHA capsules, an omega-3 product for use by pregnant and lactating women to promote brain and retinal development in babies, grew 40% to $3.9 million in 2008 (2007: $2.8 million). We believe that this is the only registered product of its type in China. Sales of the second product, ZLT Calcium powder for infant bone development, grew 77% to $1.5 million (2007: $0.8 million) as it benefited from the strong reputation and endorsement network built by ZLT DHA capsules.

Sales of the third product, ZLT Probiotics powder, a new toddler immunity product whose raw materials are imported from Denmark, grew 69% to $0.1 million.

We are actively working to broaden the ZLT range of premium quality infant nutrition and health products and will expand the range further during 2009.

## Acquisitions

We continue to appraise potential strategic acquisitions in the China healthcare market and believe good earnings enhancing opportunities exist.

Chi-Med is focusing primarily on deals with similar structure to SHPL and HBYS, which expand the capital of new joint ventures through a cash investment in return for an injection of assets by Chinese partners. We are generally targeting to take at least a 50% share in any new China joint ventures, and are seeking opportunities which are synergistic with our existing China Healthcare Division assets.


Zhi Ling Tong Calcium powder


Zhi Ling Tong Omega-3 DHA capsules

# Drug Research & Development

HMPL is dedicated to transforming scientific discoveries into innovative therapies for cancer and auto-immune diseases.

We believe that HMPL is now generally accepted as one of the leaders in China's Pharmaceutical drug discovery arena. Our strategy continues to be for HMPL to build strategic alliances with multi-national pharmaceutical groups; identify global partners with which to co-develop our lead drug candidates; and advance our in-house preclinical programs into clinical proof-of-concept ("POC") studies taking advantage of China's low cost research and development structure and vast patient population.

During 2008, we took important actions designed to set up HMPL's business for the long term. In August, we established a stand-alone employee share option scheme in Hutchison MediPharma Holdings Limited ("HMHL"), Chi-Med's wholly owned subsidiary, which holds our 100% indirect shareholding in HMPL. It is our intention that this will replace the Chi-Med employee share option scheme as the sole share-based incentive programme for HMPL employees. An initial grant of 4,542,000 share options, or 15.14% of HMHL's current total of 30,000,000 issued shares was made to more than 60 senior and middle level employees of HMPL, to acquire existing shares in HMHL at an exercise price of $1.28 per share.

This step towards stand-alone status for HMPL improves our flexibility to create and capture value by positioning HMPL as a "pure play" life science business with potential for direct external investment. This, we believe, strengthens the alignment of HMPL management and Chi-Med shareholders interests.

## Drug R&D Division performance

Drug R&D revenue grew 156% to $2.3 million (2007: $0.9 million) reflecting up-front, maintenance, and milestone payments from HMPL's collaborations with Eli Lilly, J&J and Merck. Its operating loss rose to $15.4 million (2007: -$10.1 million) as a result of the planned increased investment in HMPL's discovery organisation and preclinical small molecule programmes (HMPL-011, HMPL-012 and HMPL-013), as well as the cost of its HMPL-004 global Phase II clinical trial programmes on Crohn's disease and ulcerative colitis ("UC").

## Discovery Summary

During 2008, the discovery team selected two new high quality kinase candidates (HMPL-012 and HMPL-013) for development of cancer treatment. Together with HMPL-011, nominated in 2007, HMPL now has three Investigative New Drug ("IND") enabling preclinical programs ongoing simultaneously. These novel chemical entities were internally discovered at HMPL, synthetically produced, and are composed of a single chemical responsible for the perceived therapeutic effects.

In the auto-immune therapeutic area, HMPL-011 is a novel cytokine modulator that controls the production of pro-inflammatory cytokines and was advanced into development for rheumatoid arthritis and psoriasis. Good Manufacturing Practice production of the molecule was completed in early 2008, and IND enabling animal safety evaluation commenced in mid-2008. We expect completion of the full safety study reports by mid-2009, with IND submission for human trials shortly thereafter if warranted by the safety findings. Studies on mechanism of action and in vivo studies in preclinical animal models of HMPL-011 against other potential indications are also ongoing.

# Drug Research & Development

## Hutchison MediPharma - R&D pipeline

ONCOLOGY  AUTO-IMMUNE

| Drug Candidate | Exploratory Candidate | Preclinical Tox & CMC | Phase I | Phase II | Phase III | |
|---|---|---|---|---|---|---|
| HMPL-004 (US) (Crohn's desease) | | | | | | **ON TRACK** - 100% of patients enrolled |
| HMPL-004 (Global) (Ulcerative colitis) | | | | | | **ON TRACK** - FDA approved global multi-center Phase IIb trial in 10-07 based on China Phase II POC success. Patient enrollment on going. |
| HMPL-002 (US) (Head & neck cancer) | | | | | | **ON HOLD** - Pending both 1 and 3-year median survival data. |
| HMPL-002 (PRC) (Non small cell lung cancer) | | | | | | **ON HOLD** - Pending both 1 and 3-year median survival data. |
| HMPL-011 (Inflammation) | | | | | | **Novel cytokine modulator** - Demonstrated good efficacy in rheumatoid arthritis in animal models and pharmacokinetic properties. Going through IND enabling animal safety study. |
| HMPL-012 (Cancer) | | | | | | **Novel kinase inhibitor** - Broad-spectrum anti-tumor agent in active preclinical development. |
| HMPL-013 (Cancer) | | | | | | **Novel kinase inhibitor** - Highly selective and superiorly potent agent in active preclinical development. |

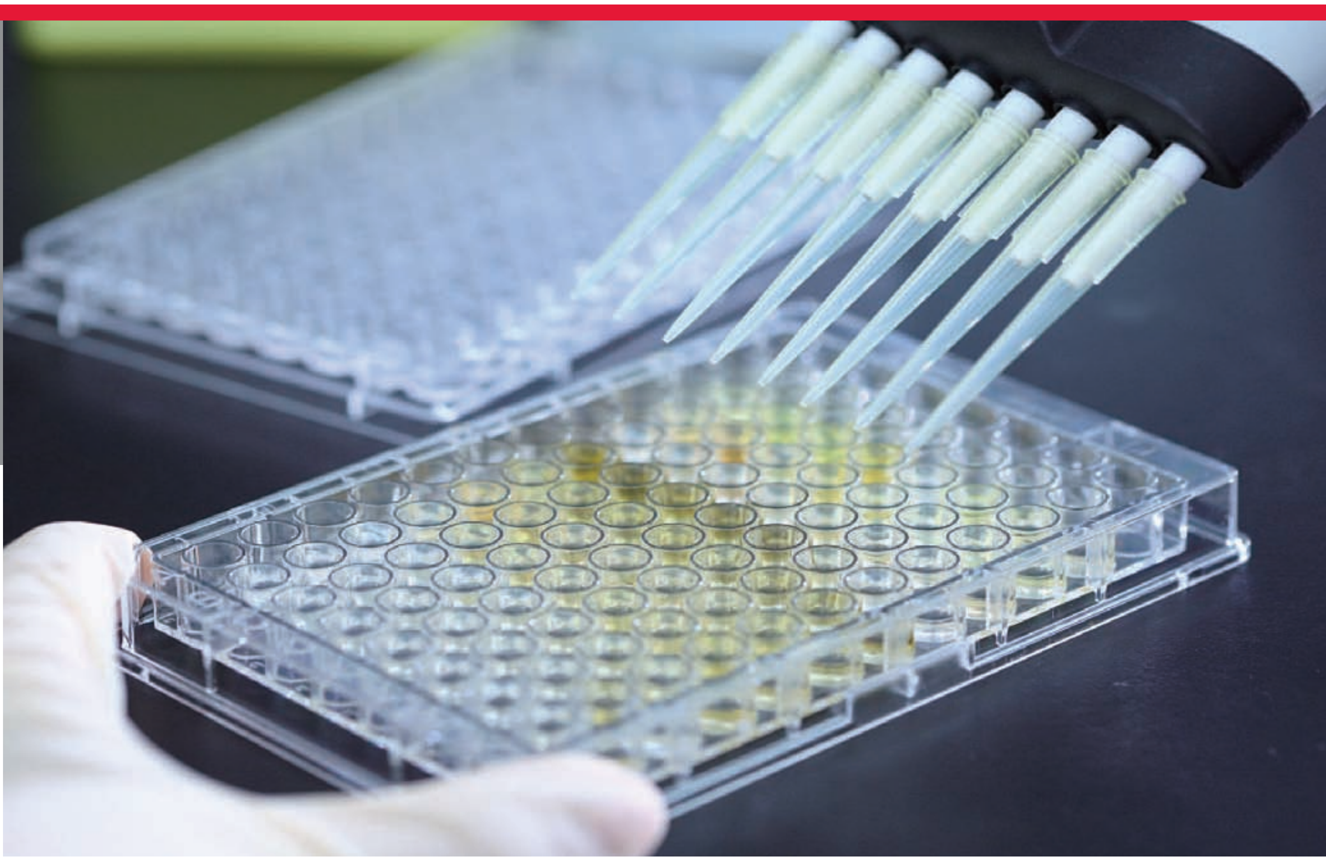
In the oncology therapeutic area, HMPL-012 entered preclinical development in 2008. HMPL-012 is a novel compound that inhibits multiple kinases crucial for tumour growth, apoptosis and invasion/metastasis. In animal efficacy studies, HMPL-012 demonstrated broad-spectrum anti-tumour activity via oral dosing. Its unique kinase profile provides a promising opportunity and potential therapeutic differentiation against existing products on the market. It is envisaged that HMPL-012 could be used as a single agent or in combination with chemotherapies for the inhibition of tumour growth as well as invasion/metastasis.

HMPL-013 is another novel chemical entity and the second drug candidate discovered internally for tumour-growth inhibition via the VEGFR (vascular endothelial growth factor) target. It is differentiated from HMPL-012 and other marketed drugs in this class by its kinase selectivity in vitro and superior potency in vivo against a variety of human xenografts. We expect the completion of the IND-enabling animal safety studies by late-2009, with regulatory submission for human clinical trials immediately following this, if warranted by the safety findings.

### Development Summary

#### *HMPL-004, Treatment for Auto-immune Disorders*

HMPL-004 is our lead drug candidate for treating inflammatory bowel diseases. It is currently in two clinical studies - a Phase II trial in the US for Crohn's disease and a global Phase IIb trial for UC.



The US Phase II trial is a multi-centre, double-blind, randomised, and placebo-controlled study in 100 male and female patients with active moderate Crohn's disease. The patient enrolment is now completed, and we expect the clinical trial outcomes by mid-2009. We are actively seeking global partners for Phase III development and beyond.

The global Phase IIb trial is a double-blind, randomised, and placebo-controlled study involving 210 patients in North America and Europe with mild-to-moderate UC. Building on the successful POC UC study conducted in China, the global trial assesses the efficacy and safety profile of HMPL-004 in a broad patient population and dose range. We anticipate finishing patient enrolment by the end of 2009.

HMPL-004 is an orally active, proprietary botanical product that acts on multiple targets in the pathogenesis of inflammation. It is a compound extracted from a Chinese herb under controlled conditions and its composition is well characterised. The anti-inflammation activity of HMPL-004 was originally identified in cell-based anti-inflammation screening at HMPL, and further confirmed in a variety of experimental animal models. During 2008, we continued to make scientific progress in understanding the drug's mechanism of action, control of its process of manufacture, and product quality in preparation for Phase III registration trials.

# Drug Research & Development

### *HMPL-002, Sensitizer for Cancer Chemo-Radiotherapy*

HMPL-002, a sensitizer used concomitantly in chemo-radiotherapy for treating cancer, has been in Phase I clinical testing in the United States for patients with locally advanced head and neck cancer and a Phase II POC study in China for patients with inoperable stage IIIA/B non-small cell lung cancer ("NSCLC").

The POC study in China of the drug candidate compared the efficacy and safety profile of chemo-radiotherapy with concomitant HMPL-002 use with standard chemo-radiotherapy for NSCLC patients. Based on the data collected and analysed to date, it has been found that the endpoint in tumour objective response (Complete Response plus Partial Response) in the locally advanced NSCLC population (Intent to Treat patients: 88) was 73.2% (30/41) in the HMPL-002 group versus 70.2% (33/47) in the control group. It is clear that the initial analysis of the study results showed no conclusive advantage in "tumour response" with oral use of HMPL-002 with chemo-radiotherapy. In the study, HMPL-002 was found to be safe and well tolerated with the most common adverse events being gastrointestinal. The progression free survival, median survival time for 1 and 3 years and time to progression are not available yet, as the one year follow-up of full patients is scheduled to complete in mid-2009.

Following this interim clinical result, we have decided to put clinical development of HMPL-002 on hold. A review of this decision will be made when both 1 and 3 year median survival data are available.

## Strategic Partnerships

A clear strand of HMPL's strategy is to seek strategic partnerships to help further enhance our discovery and development pipelines and to generate short-term revenue streams, as well as forming the basis for potential major long-term value creation through milestones and royalties on successful projects.

HMPL's first such partnership, a collaboration with Merck, has now practically concluded after reaching initial objectives. The discovery team yielded two novel hit molecules for which two milestone payments were received in 2008.

HMPL's collaboration with Eli Lilly continues to progress well and has been expanded. In late-2008 the discovery team delivered a candidate that met "lead" milestone criteria. It also developed a novel series of compounds for the same target, which Eli Lilly decided to include in the collaboration. HMPL received payments for both of these achievements and significant progress was also made for a second target, with candidate delivery expected during 2009. Building on the relationship, in November last year, HMPL and Eli Lilly expanded their 2007 collaboration by adding a new incremental program in the area of oncology.

In December 2008, one HMPL internally discovered preclinical project in the therapeutic area of inflammation was partnered out to J&J. HMPL will receive an up-front payment and J&J will support further research through success-based milestones payments as the project progresses. HMPL will also be entitled to worldwide royalties from sales of any products resulting from this collaboration.

# Consumer Products


We have started expanding Sen's main health and beauty products through third party prestige channel distribution, thereby leveraging our emerging brand and widening its geographic presence.

Since its launch in late-2002, Chi-Med's strategy for its Consumer Products Division, Sen, has been to create and develop a premium brand proposition centred on consumer health products and services derived from TCM and botanical ingredients.

Sen set out to build its brand name and reputation by establishing its own network of shops to showcase our product ranges and treatments and build direct consumer experience of the health, beauty, and lifestyle benefits that TCM can deliver. In our shops, we use TCM products and treatments, including acupuncture, acupressure, and herbal medicine, in the treatment of many conditions including inflammation related skin problems (eczema, psoriasis, acne); women's health issues (menopause, PMS); the management of pain; as well as lifestyle conditions such as stress, anxiety, depression, and addiction.

In parallel with our own shops, we have started expanding Sen's main health and beauty products through third party prestige channel distribution, thereby leveraging our emerging brand and widening its geographic presence.

# Consumer Products


## Consumer Products Division performance

Sen's sales grew 41% to $4.1 million in 2008 (2007: $2.9 million) with an operating loss of $2.6 million (2007: -$2.1 million). These results reflect both our strong sales growth and the initial launch costs of our product expansion in France.

### *Sen Medicine Company Limited ("Sen UK"): "Build brand reputation through treatments in our own shops"*

The nine central London shops/clinics performed strongly with total sales up 31% to $3.7 million (2007: $2.9 million), like-for-like sales up 17%, and despite the generally difficult late year trading conditions in London, were up 15% like-for-like in Q4 2008. Sen UK narrowed its operating loss to $1.8 million (2007: -$2.1 million). Sales growth and a positive mix effect led to aggregate shop level operating losses improving to $0.5 million (2007: -$1.0 million). The shop level gains were partially offset by central overhead costs that increased to $1.3 million (2007: $1.1 million) as we improved the operating framework of the UK business.

We believe that Sen UK currently provides the most reliable, high quality, and effective TCM consultations and treatments in London. These consultations and treatments drive margins as well as revenues. Consultation and treatment revenues were up 29% like-for-like to $2.5 million, which drove gross margins on the Sen UK business to 78% (2007: 65%). Word of mouth is growing and our base of loyal repeat customers is expanding.

### *Sen Medicine Company (France) S.A.R.L. ("Sen France"): "Expand premium consumer products line into prestige retail"*

In June 2008, we started expansion of Sen France's top 34 body care, skin care, and tea products into Perfumeries Marionnaud, Europe's largest perfumery and cosmetic retailer, which has over 1,200 shops in 13 countries, primarily in Europe. We initially launched a range of Sen products in 50 shops in June, expanding to 125 shops in mid-November 2008. Marionnaud is a part of the Hutchison Whampoa group.

Despite a difficult economic climate and the challenges of launching in a new country, we have achieved traction with Marionnaud consumer sell-out in the second half of 2008 of over $360k (over 9,800 units) equating to sales of $0.3 million for Sen France. To support the launch we invested in high quality point-of-sales materials, a Paris-based team

to manage operations including all Marionnaud central and shop level staff training, Sen France merchandisers in-store to explain the concept to shoppers and a public relations event in partnership with Marionnaud which resulted in broad-scale coverage in France's beauty press. Start-up costs also included French product registration, logistics, office and professional fees. Sen France's operating loss was therefore $0.8 million (2007: Nil).

The improvements made to our product line-up leading up to the launch in France, combined with the commercial learning since the launch, have put us in a good position to make progress in 2009.

*Current Trading and Outlook for the Group*

In 2009, sales and profit growth rates in the China Healthcare Division are running in line with last year as the China pharmaceutical market continues to show good growth. In HMPL, we are now in the process of treating the final patients in our HMPL-004 US Phase II trial on Crohn's disease and will report the result in mid-year. Early year performance on Sen UK and Sen France gives us confidence that sales will continue to grow like-for-like while operating losses narrow in both markets in 2009.

Despite the challenging global economic pressures currently evident, due to the growth markets in which we operate, strong cash position and innovative product offering, we remain confident of the overall growth prospects for Chi-Med in 2009.

**Christian Hogg**
Chief Executive Officer

13 March 2009

# Biographical Details Of Directors

## 1 Simon TO
*Executive Director and Chairman*

Mr To, aged 57, has been a Director since 2000 and an Executive Director and the Chairman since 2006. He is also the Chairman of the Remuneration Committee, a member of the Technical Committee and the Complaints Committee of the Company. He is the managing director of Hutchison Whampoa (China) Limited ("Hutchison China") and has been with Hutchison China for over twenty-eight years, building its business from a small trading company to a billion dollar investment group. He has negotiated major transactions with multinationals such as Procter & Gamble ("P&G"), Lockheed, Pirelli, Beiersdorf, United Airlines and British Airways.

Mr To's career in China spans more than thirty years and he is well known to many of the top Government leaders in China. Mr To is the original founder of Hutchison Whampoa Limited's ("Hutchison Whampoa") TCM business and has been instrumental in the acquisitions made to date. He received a First Class Honours Bachelor's Degree in Mechanical Engineering from Imperial College, London and an MBA from Stanford University's Graduate School of Business.

## 2 Christian HOGG
*Executive Director and Chief Executive Officer*

Mr Hogg, aged 43, has been an Executive Director and the Chief Executive Officer since 2006. He is also a member of the Technical Committee and the Complaints Committee of the Company. He joined Hutchison China in 2000 and has since led all aspects of the creation, implementation and management of the Company's strategy, business and listing. This includes the creation of the Company's start-up businesses and the acquisition and operational integration of assets that led to the formation of the Company's China joint ventures.

Prior to joining Hutchison China, Mr Hogg spent ten years with P&G starting in the US in Finance and then Brand Management in the Laundry and Cleaning Products Division. Mr Hogg then moved to China to manage P&G's detergent business followed by a move to Brussels to run P&G's global bleach business. Mr Hogg received a Bachelor's degree in Civil Engineering from the University of Edinburgh and an MBA from the University of Tennessee.

## 3 Shigeru ENDO
*Non-executive Director*

Mr Endo, aged 74, has been a Non-executive Director since 2008. He is chief executive officer and a director of Hutchison Whampoa Japan K.K., an executive director of Hutchison Harbour Ring Limited ("Harbour Ring"), a company listed on The Stock Exchange of Hong Kong Limited and a subsidiary of Hutchison Whampoa, and a manager (equivalent to director in the UK) of Hutchison Europe Telecommunications S.à r.l. He is also a director of Axwood Developments Limited, Hutchison Whampoa Japan Limited, Infomart Corporation and PRD Electronics Limited and was a director of TRY Electronics Japan Ltd. from 2002 to 2006. He worked for over 40 years with Mitsui, where he became senior executive managing director and a member of the main board of Mitsui and Company Ltd.

Mr Endo holds a Bachelor of Arts degree in Economics from Keio University. During his career, Mr Endo, a Japanese citizen and fluent English and Mandarin speaker, has managed large-scale business operations in Japan, China and the United States.

## 4 Christian SALBAING
*Non-executive Director*

Mr Salbaing, aged 59, has been a Non-executive Director since 2006. He is the deputy chairman of Hutchison Whampoa (Europe) Limited, European headquarters company of Hutchison Whampoa for its businesses in Europe. He is also a manager of Hutchison Europe Telecommunications S.à r.l. Mr Salbaing was previously a partner at Freshfields Bruckhaus Deringer, an international law firm. Mr Salbaing represents Hutchison Whampoa's businesses across Europe, in particular with the European Commission and member governments and in relation to regulatory and public affairs matters. He is a member of the ITU Telecom Board.

Mr Salbaing received an LL.L. degree in Civil Law from the University of Montreal in 1970 and a Juris Doctor degree from the University of San Francisco in 1974. He is a member of the Bars of Quebec, California and Paris.

## 5 Edith SHIH
*Non-executive Director and Company Secretary*

Ms Shih, aged 57, has been a Non-executive Director since 2006 and the Company Secretary since 2000. She is also a member of the Complaints Committee of the Company. She is the head group general counsel and company secretary of Hutchison Whampoa and an executive director of Harbour Ring, director of Hutchison International Limited, as well as director and company secretary of numerous companies in the Hutchison Whampoa group. Ms Shih has been employed by Hutchison Whampoa since 1991 and oversees all legal, regulatory and corporate secretarial affairs of the Hutchison Whampoa group.

Ms Shih received a Bachelor of Science degree in Education and a Master of Arts degree from the University of the Philippines and a Master of Arts degree and a Master of Education degree from Columbia University, New York. Ms Shih is a qualified solicitor in Hong Kong, England and Wales and Victoria, Australia and a Fellow of both The Institute of Chartered Secretaries and Administrators and The Hong Kong Institute of Chartered Secretaries.

## 6 Michael HOWELL
*Independent Non-executive Director*

Mr Howell, aged 61, has been an Independent Non-executive Director since 2006. He is also the Chairman of the Audit Committee and a member of the Remuneration Committee and the Complaints Committee of the Company. Until 2006, he was chief executive officer of tie (Transport Initiatives Edinburgh) Ltd., a company responsible for over £1.5 billion in transportation projects in Scotland including a new tram system and an airport rail link for Edinburgh. Mr Howell's thirty year career has been primarily in manufacturing, distribution and transportation services where, after beginning his career at British Leyland, Mr Howell went on to hold senior positions at Cummins Engine and General Electric in the USA and Europe. Mr Howell holds multiple directorships in both private and public companies in Europe and the USA. He is currently the chairman of the City and Guilds of London Institute, and chairman of Evo Electric Limited ("EEL").

Mr Howell has received a Masters degree in Economics/Engineering from Trinity College, Cambridge and MBAs from INSEAD and Harvard University.

## 7 Christopher HUANG
*Independent Non-executive Director*

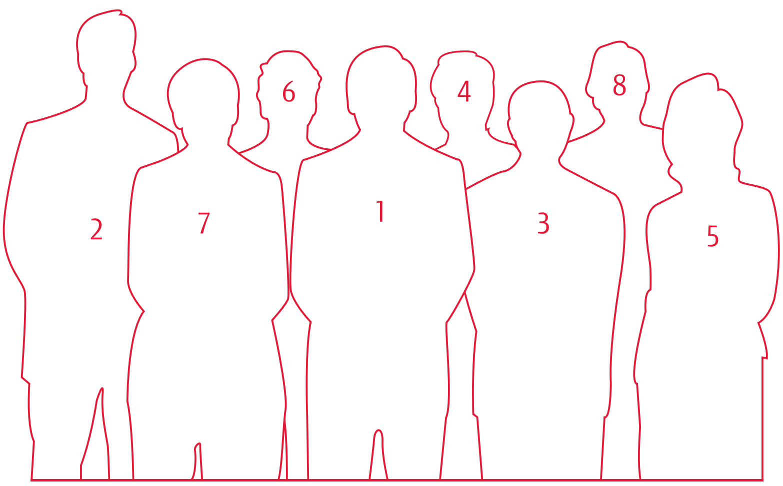
Professor Huang, aged 58, has been an Independent Non-executive Director since 2006. He is also the Chairman of the Technical Committee and a member of the Audit Committee of the Company. He is currently Professor of Cell Physiology, and Fellow and director of Studies in Medicine at Murray Edwards College, University of Cambridge, UK. Professor Huang has spent over twenty years in academia and research in the field of cellular and systems physiology. He has authored over 200 publications in the form of monographs, books, papers and articles whilst pursuing research collaborations with major pharmaceutical companies and holds editorships of *Biological Reviews, the Journal of Physiology* and *Europace*.

Professor Huang completed his Bachelor's degrees in Physiological Sciences (B.A.) and Clinical Medicine (B.M., B.Ch.) at The Queen's College, Oxford, and his postgraduate (Ph.D.) degree at the University of Cambridge. He has also been awarded higher medical (D.M.) and scientific (D.Sc.) degrees by both Oxford and Cambridge.

## 8 Christopher NASH
*Independent Non-executive Director*

Mr Nash, aged 50, has been an Independent Non-executive Director since 2006 and was appointed as Senior Independent Director in September 2006. He is also a member of the Audit Committee and the Remuneration Committee of the Company. He is also a non-executive director of NTR plc, EEL and Zenergy Power plc. Mr Nash has had about thirty years' business career during which he was senior vice president and group head of strategy and corporate finance at Global Crossing Ltd., where he also served on the management board and several divisional boards. In the mid-1990s he was group head of corporate finance at Cable & Wireless Plc., and before that a director of North West Water International Ltd. Earlier in his career Mr Nash worked for S.G. Warburg and Co. Ltd. and also spent some time in the venture capital sector. During his career, Mr Nash has spent significant periods of time in Asia.

Mr Nash received a Bachelor's degree in Civil Engineering from Imperial College, London and an MBA from Manchester Business School.



# Report Of The Directors

The Directors have pleasure in submitting to shareholders their report and statement of audited accounts for the year ended 31 December 2008.

## PRINCIPAL ACTIVITIES

The principal activity of the Company is that of a holding company of a pharmaceutical and healthcare group whose main country of operation is China. It engages in research, development, manufacturing and sales of pharmaceuticals, health supplements and other consumer health and personal care products derived from traditional Chinese medicine and botanical ingredients.

## BUSINESS REVIEW

A detailed review of the performance, business activities and future development of the Group are set out in the Chairman's Statement and the Chief Executive Officer's Statement.

## RESULTS

The Consolidated Profit and Loss Account is set out on page 44 and shows the Group's results for the year ended 31 December 2008.

## DIVIDENDS

No interim dividend for the year ended 31 December 2008 was declared and the Directors do not recommend the payment of a final dividend for the year ended 31 December 2008.

## RESERVES

Movements in the reserves of the Group during the year are set out in the Consolidated Statement of Changes in Equity on page 46.

## NON-CURRENT ASSETS

Particulars of the movements of non-current assets of the Group are set out in notes 14 to 19 of the Consolidated Balance Sheet.

## SHARE CAPITAL

Details of the share capital of the Company are set out in note 23 of the Consolidated Balance Sheet.

## DIRECTORS

The Directors of the Company as at 31 December 2008 were:

### Executive Directors:

Mr Simon To
Mr Christian Hogg

### Non-executive Directors:

Mr Shigeru Endo
Mr Christian Salbaing
Ms Edith Shih

### Independent Non-executive Directors:

Mr Michael Howell
Prof Christopher Huang
Mr Christopher Nash

During the year, Mr Shigeru Endo was appointed as Non-executive Director of the Company on 1 June 2008 and Mr Patrick Wan resigned as Executive Director of the Company on 8 October 2008.

Ms Edith Shih, Prof Christopher Huang and Mr Christopher Nash will retire by rotation at the forthcoming annual general meeting under the provisions of Article 91(1) of the Articles of Association of the Company and, being eligible, will offer themselves for re-election. Mr Shigeru Endo shall hold office until the forthcoming annual general meeting under the provisions of Article 90(3) of the Articles of Association of the Company and, being eligible, will offer himself for re-election.

The Directors' biographical details are set out on pages 28 to 29.

## DIRECTORS' INTERESTS IN SHARES

As at 31 December 2008, the interests in the shares of the Company held by the Directors and their families were as follows:

| Name of Directors | Number of Ordinary Shares held |
|---|---|
| Christian Hogg | 270,000 |
| Michael Howell | 43,000 |
| Christopher Nash | 18,000 |

## SHARE OPTION SCHEMES AND DIRECTORS' RIGHTS TO ACQUIRE SHARES

### (i) Share option scheme of the Company

On 4 June 2005, the Company adopted a share option scheme (the "Share Option Scheme"), which was subsequently amended by the Board of Directors of the Company on 21 March 2007. Pursuant to the Share Option Scheme, the Board of Directors of the Company may, at its discretion, offer any employees and directors (including Executive and Non-executive directors but excluding Independent Non-executive directors) of the Company, holding companies of the Company and any of their subsidiaries or affiliates, and subsidiaries or affiliates of the Company options to subscribe for shares of the Company.

The following share options were outstanding under the Share Option Scheme during the year ended 31 December 2008:

| Name or category of participant | Effective date of grant of share options | Number of share options held at 1 January 2008 | Granted during 2008 | Exercised during 2008 | Expired/ cancelled/ surrendered during 2008 | Number of share options held at 31 December 2008 | Exercise period of share options | Exercise price of share options £ |
|---|---|---|---|---|---|---|---|---|
| Christian Hogg | 19.5.2006 (1), (2) | 768,182 | - | - | - | 768,182 | 19.5.2006 to 3.6.2015 | 1.090 |
| 6 employees in aggregate | 19.5.2006 (1), (2) | 870,605 | - | - | (266,922) | 603,683 | 19.5.2006 to 3.6.2015 | 1.090 |
| 2 employees in aggregate | 11.9.2006 (2) | 120,810 | - | - | (40,352) | 80,458 | 11.9.2006 to 18.5.2016 | 1.715 |
| 1 employee | 23.3.2007 (3) | 25,606 | - | - | (17,071) | 8,535 | 23.3.2007 to 22.3.2017 | 1.750 |
| 8 employees in aggregate | 18.5.2007 (3) | 311,146 | - | - | (220,848) | 90,298 | 18.5.2007 to 17.5.2017 | 1.535 |
| 1 employee | 24.8.2007 (3) | 322,608 | - | - | (66,548) | 256,060 | 24.8.2007 to 23.8.2017 | 1.685 |
| 1 employee | 25.8.2008 (4) | N/A | 256,146 | - | - | 256,146 | 25.8.2008 to 24.8.2018 | 1.260 |
| Total: | | 2,418,957 | 256,146 | - | (611,741) (5) | 2,063,362 | | |

Notes:

(1) The share options were granted on 4 June 2005, conditionally upon the Company's admission which took place on 19 May 2006.

(2) The share options granted to certain founders of the Company are subject to, amongst other relevant vesting criteria, the vesting schedule of 50% on 19 May 2007 and 25% on each of 19 May 2008 and 19 May 2009. The share options granted to non-founders of the Company are subject to, amongst other relevant vesting criteria, the vesting schedule of one-third on each of 19 May 2007, 19 May 2008 and 19 May 2009.

(3) The share options granted are subject to, amongst other relevant vesting criteria, the vesting schedule of one-third on each of the first, second and third anniversaries of the date of grant of share options.

(4) The share options granted are subject to, amongst other relevant vesting criteria, the vesting schedule of 25% on each of the first, second, third and fourth anniversaries of the date of grant of share options.

(5) A total of 467,587 unvested share options of the Company held by the employees of Hutchison MediPharma Limited were surrendered by consent. In addition, 144,154 share options of the Company held by certain employees of the Group were cancelled during the year following the cessation of their employment pursuant to the Company's Share Option Scheme.

### (ii) Share option scheme for existing shares of Hutchison MediPharma Holdings Limited ("HMHL")

On 6 August 2008, HMHL, a direct wholly-owned subsidiary of the Company, adopted a share option scheme (the "HMHL Share Option Scheme") pursuant to which any employee or director of HMHL and any of its subsidiaries and affiliates is eligible to participate in the HMHL Share Option Scheme subject to the discretion of the board of directors of HMHL. An initial grant of 4,542,000 options to acquire existing shares held by the Company in HMHL (representing approximately 15.14% of HMHL's existing issued share capital) has been made to more than 60 senior and middle level employees of Hutchison MediPharma Limited ("HMPL"), an indirect wholly-owned subsidiary of HMHL, at an exercise price of USD1.28 per share. A total of 467,587 unvested share options of the Company were surrendered by some of those HMPL employees by consent.

It is the Group's intention that the HMHL Share Option Scheme will replace the Company's Share Option Scheme as the sole share-based incentive programme for HMPL employees.

The following share options were outstanding under the HMHL Share Option Scheme during the year ended 31 December 2008:

| Category of participant | Effective date of grant of share options | Number of share options held at 1 January 2008 | Granted during 2008 | Exercised during 2008 | Expired/ cancelled/ surrendered during 2008 | Number of share options held at 31 December 2008 | Exercise period of share options | Exercise price of share options US$ |
|---|---|---|---|---|---|---|---|---|
| 64 employees in aggregate | 6.8.2008 | N/A | 4,542,000 | - | (14,000) | 4,528,000 | 6.8.2008 to 5.8.2014 | 1.28 |

Note:

The share options granted are subject to, amongst other relevant vesting criteria, the vesting schedule of 25% on each of the first, second, third and fourth anniversaries of the date of grant of share options.

## SIGNIFICANT SHAREHOLDINGS

As at 23 March 2009, being the latest practicable date prior to the publication of this report, according to the records of the Company, the following holders held interests in 3% or more of the issued share capital of the Company:-

| Names | Number of Ordinary Shares held | Approximate % of Issued Share Capital |
|---|---|---|
| Hutchison Healthcare Holdings Limited[1] ("HHHL") | 36,666,667 | 71.6% |
| Computershare Company Nominees Limited ("CCNL") | 14,468,635 | 28.2% |
| *Depositary Interest held under CCNL:* | | |
| Apollo Nominees Limited | 4,324,592 | 8.4% |
| Chase Nominees Limited | 2,010,648 | 3.9% |
| UBS Investment Bank | 4,324,592 | 8.4% |
| Cazenove Capital Management Limited | 2,265,305 | 4.4% |

Note:

(1) HHHL is a private company registered in the British Virgin Islands and carries on business as a holding company. HHHL is an indirect wholly owned subsidiary of Hutchison Whampoa Limited which is registered in Hong Kong.

## AUDITOR

The accounts have been audited by PricewaterhouseCoopers who will retire and, being eligible, will offer themselves for re-appointment.

## ANNUAL GENERAL MEETING

The annual general meeting ("AGM") of the Company will be held on Friday, 8 May 2009 at 11:00 am (UK time) at Citigate Dewe Rogerson, 3 London Wall Buildings, London, EC2M 5SY. Details of the resolutions proposed are set out in the Notice of the AGM.

By Order of the Board

**Edith Shih**
*Director and Company Secretary*

13 March 2009

# Corporate Governance Report

The Company strives to attain and maintain the highest standards of corporate governance as it believes that effective corporate governance practices are fundamental to enhancing shareholder value and safe-guarding shareholder interests. The Company has accordingly adopted sound corporate governance principles that emphasise a quality board of Directors (the "Board"), effective internal control, stringent disclosure practices and transparency and accountability to all stakeholders. It is, in addition, committed to continuously improving these practices and inculcating an ethical corporate culture. The Company has applied the principles of the Combined Code on Corporate Governance (the "Code") notwithstanding that the Company's shares are admitted to trade on the Alternative Investment Market ("AIM") and it is therefore not required to comply with the Code.

Set out below are the corporate governance practices adopted by the Company.

## THE BOARD

The Board is responsible for directing the strategic objectives of the Company and overseeing the management of the business. Directors are charged with the task of promoting the success of the Company and making decisions in the best interest of the Company. The Board is satisfied that it meets the Code's requirement for effective operation.

The Board, led by the Chairman, Mr Simon To, approves and monitors the Group's long term objectives and commercial strategies, annual operating and capital expenditure budgets and business plans, evaluating the performance of the Company and supervising the management of the Company (the "Management"). Management is responsible for the day-to-day operations of the Group under the leadership of the Chief Executive Officer.

As at 31 December 2008, the Board comprised eight Directors, including an Executive Chairman, Chief Executive Officer and Executive Director, three Non-executive Directors and three Independent Non-executive Directors (one of whom is Senior Independent Director) following the appointment of one Non-executive Director on 1 June 2008 and the resignation of an Executive Director on 8 October 2008. Biographical details of the Directors are set out on pages 28 to 29.

For a Director to be considered independent, the Board must be satisfied that the Director does not have any direct or indirect material relationship with the Group. In determining the independence of Directors, the Board follows the requirements set out in the Code.

The roles of the Chairman are separate from that of the Chief Executive Officer. Such division of responsibilities helps to reinforce their independence and accountability.

The Chairman is responsible for the effective conduct of the Board, ensuring that it as a whole plays an effective role in the development and determination of the Group's strategy and overall commercial objectives and acts as the guardian of the Board's decision-making processes. He is responsible for setting the agenda for each Board meeting, taking into account, where appropriate, matters proposed by Directors for inclusion in the agenda. He also ensures that the Board receives accurate, timely and clear information on the Group's performance, the issues, challenges and opportunities facing the Group and matters reserved to it for decision. With the support of Executive Directors and the Company Secretary, the Chairman ensures that the Board complies with approved procedures, including the schedule of Reserved Matters to the Board for its decision and Terms of Reference of all Board Committees. The Board, under the leadership of the Chairman, has adopted good corporate governance practices and procedures and taken appropriate steps to provide effective communication with shareholders.

The Chief Executive Officer, Mr Christian Hogg, is responsible for managing the businesses of the Group, formulating and developing the Group's strategy and overall commercial objectives in close consultation with the Chairman and the Board. With the executive team, the Chief Executive Officer implements the decisions of the Board and its Committees. He maintains a dialogue with the Chairman to keep him fully informed of all major business development and issues. He is also responsible for ensuring that the development needs of senior management reporting to him are identified and met as well as leading the communication programme with shareholders.

The Board meets regularly. Between scheduled meetings, senior management of the Group provides information regularly to Directors on the activities and development of the Group. Throughout the year, Directors participate in the consideration and approval of routine and operational matters of the Company by way of circular resolutions with supporting explanatory materials, supplemented by additional verbal and/or written information or notification from the Company Secretary and other executives as and when required. Whenever warranted, additional Board meetings are held. In addition, Directors have full access to information on the Group and independent professional advice at all times whenever deemed necessary by the Directors.

With respect to regular meetings of the Board, Directors receive written notice of the meetings at least 14 days in advance and an agenda with supporting Board papers no less than 3 days prior to the meetings. With respect to other meetings, Directors are given as much notice as is reasonable and practicable in the circumstances.

The Board held four meetings in 2008 with 100% attendance.

| **Position** | **Name of Directors** | **Attended / Eligible to attend** |
|---|---|---|
| Chairman | Simon To | 4/4 |
| Executive Directors: | Christian Hogg *(Chief Executive Officer)* | 4/4 |
| | Patrick Wan (1) | 3/3 |
| Non-executive Directors: | Shigeru Endo (2) | 2/2 |
| | Christian Salbaing | 4/4 |
| | Edith Shih | 4/4 |
| Independent Non-executive Directors: | Michael Howell | 4/4 |
| | Christopher Huang | 4/4 |
| | Christopher Nash | 4/4 |

Notes

(1) Resigned as Executive Director on 8 October 2008.

(2) Appointed as Non-executive Director on 1 June 2008.

During the year, the Chairman held two meetings with Non-executive Directors without Executive Directors with full attendance to review the performance of the Executive Directors. The Senior Independent Director, Mr Christopher Nash, also held a meeting with Non-executive Directors without the presence of the Chairman with full attendance for the appraisal of the Chairman's performance.

In addition, an evaluation of the performance of the Board and its Committees was conducted by questionnaire. The objective of such evaluation is to ensure that the Board, its Committees and each individual Director continued to act effectively in fulfilling the duties and responsibilities expected of them.

# Corporate Governance Report

All Non-executive Directors are engaged on service contracts which are automatically renewed for successive 12 month periods unless terminated by written notice given by either party. The Chairman of the Board is of the view that the performance of each of the Non-executive Directors continues to be effective and they all demonstrate commitment to their role as a Non-executive Director. All Directors are subject to re-election by shareholders at the annual general meeting following their appointment and at least every three years on a rotational basis. Save as mentioned herein, there are no existing or proposed service contracts between any of the Directors and the Company which cannot be terminated by the Company within 12 months without payment of compensation. Where vacancies arise at the Board, candidates are proposed and put forward to the Board for consideration and approval, with the objective of appointing to the Board individuals with expertise in the businesses of the Group and leadership qualities so as to complement the capabilities of the existing Directors thereby enabling the Company to retain as well as improve its competitive position.

Upon appointment to the Board, each Director is provided with a comprehensive induction to the Group's businesses by senior executives. Continuing education and information are provided to Directors regularly to help ensure that Directors are apprised of the latest changes in the commercial, legal and regulatory environment in which the Group conducts its businesses.

## DIRECTORS' RESPONSIBILITY FOR THE ACCOUNTS

The following statement, which sets out the responsibility of Directors in relation to the financial statements, should be read in conjunction with, but distinguished from, the Independent Auditor's Report on page 43 which acknowledges the reporting responsibility of the Group's Auditor.

### Annual Report and Accounts

The Directors are responsible for the preparation of the Annual Report and Financial Statements of the Company to ensure that these financial statements give a fair presentation in accordance with Cayman Islands Companies Law and the applicable accounting standards.

### Accounting Policies

The Directors consider that in preparing the financial statements, the Group has applied appropriate accounting policies that are consistently adopted and made judgements and estimates that are reasonable and prudent in accordance with the applicable accounting standards.

### Accounting Records

The Directors are responsible for ensuring that the Group keeps accounting records which disclose the financial position of the Group upon which financial statements of the Group could be prepared in accordance with the Group's accounting policies.

### Safeguarding Assets

The Directors are responsible for taking all reasonable and necessary steps to safeguard the assets of the Group and to prevent and detect fraud and other irregularities within the Group.

### Going Concern

The Directors, having made appropriate enquiries, consider that the Group has adequate resources to continue in operational existence for the foreseeable future and that, for this reason, it is appropriate to adopt the going concern basis in preparing the financial statements.

## COMPANY SECRETARY

The Company Secretary, Ms Edith Shih, is responsible to the Board for ensuring that Board procedures are followed and Board activities are efficiently and effectively conducted. These objectives are achieved through the adherence to proper Board processes and the timely preparation and dissemination to Directors and Board Committees comprehensive agendas and papers.

The Company Secretary is responsible for ensuring that the Board is fully apprised of the relevant legislative, regulatory and corporate governance developments relating to the Group and that it takes these into consideration when making decisions for the Group. The Company Secretary is also directly responsible for the Group's compliance with all obligations of the AIM Rules for Companies ("AIM Rules"), including publication and dissemination of annual reports and interim reports within the periods laid down in the AIM Rules, timely dissemination to the shareholders and the market of announcements and information relating to the Group and assisting in the notification of Directors' dealings in securities of the Group.

The Company Secretary advises the Directors on their obligations for disclosure of interests in securities, related party transactions and price-sensitive information and ensures that the standards and disclosures required by the AIM Rules are observed and, where required, reflected in the Report of the Directors in the Annual Report.

In relation to related party transactions, regular seminars are conducted for legal counsels and executives from business units within the Group to ensure that such transactions are handled in compliance with the AIM Rules. Detailed analyses are performed on all potential related party transactions to ensure full compliance and for Directors' consideration.

## BOARD COMMITTEES

The Company has established an Audit Committee, a Remuneration Committee, a Technical Committee and a Complaints Committee.

### Audit Committee

The Audit Committee comprises three Independent Non-executive Directors with recent and relevant financial experience. It is chaired by Mr Michael Howell with Professor Christopher Huang and Mr Christopher Nash as members. None of the Committee Members is related to the Company's external auditors.

Under the terms of reference of the Audit Committee, the Committee is required to review the Group's interim and final results and annual financial statements, oversee the relationship between the Company and its external auditors, monitor and review the effectiveness of the Company's internal audit function in the context of the Company's overall risk management systems giving due consideration to laws and regulations and the provisions of the Code. The Committee is authorised to obtain, at the Company's expense, external legal or other professional advice on any matters within its terms of reference.

The terms of reference of the Audit Committee adopted by the Board are published on the Company's website.

The Audit Committee held three meetings in 2008 with 100% attendance.

| **Name of Members** | **Attended / Eligible to attend** |
|---|---|
| Michael Howell *(Chairman)* | 3/3 |
| Christopher Huang | 3/3 |
| Christopher Nash | 3/3 |

# Corporate Governance Report

*Financial Statements*

The Audit Committee meets with the senior management of the Company from time to time to review the interim and final results and the Interim Report and Annual Report of the Company. It considers and discusses the reports and presentations of Management and the Group's internal and external auditors, with a view of ensuring that the Group's consolidated financial statements are prepared in accordance with International Financial Reporting Standards. It also meets with the Group's principal external auditor, PricewaterhouseCoopers ("PwC"), to consider their reports on the scope and outcome of their independent review of the interim financial report and their annual audit of the consolidated financial statements.

*External Auditors*

The Audit Committee reviews and monitors the external auditors' independence, objectivity and effectiveness of the audit process and holds meetings with PwC to consider the scope of their audit, approve their fees, and the scope and appropriateness of non-audit services, if any, to be provided by them. The Audit Committee also makes recommendations to the Board on the appointment and retention of the external auditors.

The Group's policy regarding the engagement of PwC for the various services listed below is as follows:

- Audit services – includes audit services provided in connection with the audit of the consolidated financial statements. All such services are to be provided by external auditors.

- Audit related services – includes services that would normally be provided by an external auditor but not generally included in the audit fees, for example, audits of the Group's pension plans, due diligence and accounting advice related to mergers and acquisitions, internal control reviews of systems and/or processes, and issuance of special audit reports for tax or other purposes. The external auditors are to be invited to undertake these services that they must or are best placed to undertake in their capacity as auditors.

- Taxation related services – includes all tax compliance and tax planning services, except for those services which are provided in connection with the audit. The Group uses the services of the external auditors where they are best suited. All other significant taxation related work is undertaken by other parties as appropriate.

- Other services – includes, for example, audits or reviews of third parties to assess compliance with contracts, risk management diagnostics and assessments, and non-financial systems consultations. The external auditors are also permitted to assist management and the Group's internal auditors with internal investigations and fact-finding into alleged improprieties. These services are subject to specific approval by the Audit Committee.

- General consulting services – the external auditors are not eligible to provide services involving general consulting work.

For the year ended 31 December 2008, the fees paid to PwC were for both audit and non-audit services. The non-audit services were mainly related to the tax compliance services which amounted to approximately USD51,000. It is considered that the non-audit service fees are immaterial and the services provided are in no way impede the independence of the auditor.

*Review of Risk Management and Internal Control*

The Audit Committee assists the Board in meeting its responsibility for maintaining an effective system of internal control. It reviews the process by which the Group evaluates its control environment and risk assessment process, and the way in which business and control risks are managed. It also reviews with the internal auditors of the Group's holding company the work plan for their audits together with their resource requirements and considers the report of the Group's internal auditors to the Audit Committee on the effectiveness of internal controls in the Group business operations. In addition, it also receives the report from the Company Secretary on the Group's compliance status on regulatory requirements. These reviews and reports are taken into consideration by the Audit Committee when it makes its recommendation to the Board for approval of the consolidated financial statements for the year.

## Remuneration Committee

The Remuneration Committee comprises three members, chaired by the Chairman Mr Simon To with Messrs Michael Howell and Christopher Nash, both Independent Non-executive Directors, as members who possess experience in human resources and personnel emoluments. Mr To has experience in the traditional Chinese medicine industry as well as expertise in human resources and personnel in China. The Remuneration Committee meets towards the end of each year for the determination of the remuneration package of Executive Directors and senior management of the Group and during the year to consider share options grant and other remuneration related matters.

The responsibility of the Remuneration Committee is to assist the Board in achieving its objective of attracting, retaining and motivating people of the highest calibre and experience needed to shape and execute strategy across the Group's substantial and diverse international business operations. It assists the Group in the administration of a fair and transparent procedure for setting remuneration policies including assessing the performance of Executive Directors and senior executives of the Group and determining their remuneration packages.

The terms of reference of the Remuneration Committee adopted by the Board are published on the Company's website.

The remuneration of Mr Christian Hogg, the Executive Director, and senior executives is determined with reference to the performance and profitability of the Group as well as remuneration benchmarks from other local and international companies and prevailing market conditions. Senior management also participates in bonus awards determined in accordance with the performance of the Group and the individual's performance. The Chairman, Mr Simon To, does not receive performance related remuneration from the Company and is remunerated through his service agreement. All Non-executive Directors have entered into service agreements with the Company and are remunerated with fixed fees as determined by the Board.

The Remuneration Committee held one meeting in 2008 with 100% attendance.

The Directors received the following remuneration from the Company during the year:

| **Name of Directors** | **Salary and fees** | **Bonus** | **Taxable benefits** | **Pension contributions** | **Share option benefits** (6) | **Total** |
|---|---|---|---|---|---|---|
| | US$ | US$ | US$ | US$ | US$ | US$ |
| *Executive Directors:* | | | | | | |
| Simon To (1) | 18,814 | - | - | - | - | 18,814 |
| Christian Hogg (2) | 313,022 | 256,410 | 14,623 | 20,615 | 298,375 | 903,045 |
| Patrick Wan (3) | 14,445 | - | - | - | - | 14,445 |
| *Non-executive Directors:* | | | | | | |
| Shigeru Endo (4) | 11,001 | - | - | - | - | 11,001 |
| Christian Salbaing (5) | 18,814 | - | - | - | - | 18,814 |
| Edith Shih (4) | 18,814 | - | - | - | - | 18,814 |
| *Independent Non-executive Directors:* | | | | | | |
| Michael Howell | 45,154 | - | - | - | - | 45,154 |
| Christopher Huang | 45,154 | - | - | - | - | 45,154 |
| Christopher Nash | 45,154 | - | - | - | - | 45,154 |
| **Aggregate emoluments** | 530,372 | 256,410 | 14,623 | 20,615 | 298,375 | 1,120,395 |

Notes

(1) Such Director's fees were paid to Hutchison Whampoa (China) Limited.

(2) Emoluments paid include Director's fees of US$18,814.

(3) Such Director's fees were paid up to 7 October 2008 as he resigned as Executive Director on 8 October 2008.

(4) Such Director's fees were paid to Hutchison Whampoa Limited.

(5) Such Director's fees were paid to Hutchison Whampoa (Europe) Limited

(6) Share option benefits represent the fair value of share options granted under the Company's share option scheme, which is calculated in accordance with the methodology disclosed in note 2(s)(ii) to the accounts. This methodology does not take into account of the actual share price at the date of exercise and whether the share options have been exercised. The significant inputs to the valuation model are disclosed in note 23(b)(i) to the accounts and details of the share options granted are set out on pages 31 and 78 of this Annual Report.

### Technical Committee

The Technical Committee comprises three members, chaired by Professor Christopher Huang with Messrs Simon To and Christian Hogg, both Executive Directors, as members. The Technical Committee members consider from time to time matters relating to the technical aspects of the business and in research and development. It also invites such executives as it thinks fit to attend meetings as and when required.

The terms of reference of the Technical Committee adopted by the Board are published on the Company's website.

The Technical Committee held two meetings in 2008 with 100% attendance.

| Name of Members | Attended/Eligible to attend |
|---|---|
| Christopher Huang *(Chairman)* | 2/2 |
| Simon To | 2/2 |
| Christian Hogg | 2/2 |

### Complaints Committee

The Complaints Committee comprises Messrs Simon To, Christian Hogg, Michael Howell and Edith Shih as members. The Complaints Committee was established mainly for processing complaints and concerns raised by employees of the Group regarding the business and operations of the Group through the dedicated phone line and website. The members also monitor the investigative actions taken by the Company and the outcome of investigations.

## INTERNAL CONTROL AND GROUP RISK MANAGEMENT

### Introduction

The Board has overall responsibility for the Group's system of internal control and assessment and management of risks.

In meeting its responsibility, the Board seeks to increase risk awareness across the Group's business operations and has put in place policies and procedures, including parameters of delegated authority, which provide a framework for the identification and management of risks. It also reviews and monitors the effectiveness of the systems of internal control to ensure that the policies and procedures in place are adequate. Reporting and review activities include the review by Executive Directors and the Board and approval of detailed operational and financial reports, budgets and plans provided by the management of the business operations, review by the Board of actual results against the budgets, reviews by the Audit Committee of the ongoing work of the Internal Audit and Risk Management Departments of the Group's holding company, as well as regular business reviews by Executive Directors and the executive management team of each core business division.

Whilst these procedures are designed to identify and manage risks that could adversely impact the achievement of the Group's business objectives, they do not provide absolute assurance against material mis-statement, errors, losses or fraud.

## Internal Control Environment

The Board is overall responsible for monitoring the operations of the businesses within the Group. Executive Directors are appointed to the boards of all material operating subsidiaries and associates for monitoring those companies, including attendance at board meetings, review and approval of business strategies, budgets and plans, and setting of key business performance targets. The executive management team of each core business division is accountable for the conduct and performance of each business in the division within the agreed strategies and similarly the management of each business is accountable for its conduct and performance.

The Group's internal control procedures include a comprehensive system for reporting information to the executive management teams of each core business and the Executive Directors.

Business plans and budgets are prepared annually by the management of individual businesses and subject to review and approval by both the executive management teams and the Executive Directors as part of the Group's five-year corporate planning cycle. Reforecasts for the current year are prepared on a quarterly basis, reviewed for variances to the budget and for approval. When setting budgets and reforecasts, management identifies, evaluates and reports on the likelihood and potential financial impact of significant business risks.

The Executive Directors review monthly management reports on the financial results and key operating statistics of each business and discuss with the executive management team and senior management of business operations to review these reports, business performance against budgets, forecasts, significant business risk sensitivities and strategies. In addition, financial controllers of the executive management teams of each of the major business discuss with the representatives of the Finance Department to review monthly performance against budget and forecast, and to address accounting and finance related matters.

The Finance Department has established guidelines and procedures for the approval and control of expenditures. Operating expenditures are subject to overall budget control and are controlled within each business with approval levels set by reference to the level of responsibility of each executive and officer. Capital expenditures are subject to overall control within the annual budget review and approval process, and more specific control and approval prior to commitment by the Finance Department or other Executive Directors are required for unbudgeted expenditures and material expenditures within the approved budget. Quarterly reports of actual versus budgeted and approved expenditures are also reviewed.

The General Manager of the Internal Audit Department of the Group's holding company, reporting directly to the Audit Committee, provides independent assurance as to the existence and effectiveness of the risk management activities and controls in the Group's business operations in various countries. Using risk assessment methodology and taking into account the dynamics of the Group's activities, internal audit derives its yearly audit plan which is reviewed by the Audit Committee, and reassessed during the year as needed to ensure that adequate resources are deployed and the plan's objectives are met. Internal Audit Department of the Group's holding company is responsible for assessing the Group's internal control system, formulating an impartial opinion on the system, and reporting its findings to the Audit Committee and the senior management concerned as well as following up on all reports to ensure that all issues have been satisfactorily resolved. In addition, a regular dialogue is maintained with the Group's external auditors so that they are aware of the significant factors which may affect their respective scope of work.

Depending on the nature of business and risk exposure of individual business units, the scope of work performed by the internal audit function includes financial and operations reviews, recurring and surprise audits, fraud investigations and productivity efficiency reviews.

Reports from the external auditors on internal controls and relevant financial reporting matters are communicated with the General Manager of the Internal Audit Department of the Group's holding company and, as appropriate, with the financial controller of the relevant executive management team. These reports are reviewed and appropriate actions are taken.

## Group Risk Management

The Chief Executive Officer and the Risk Management Department of the Group's holding company have the responsibility of developing and implementing risk mitigation strategies including the deployment of insurance to transfer the financial impact of risks. The General Manager of the Risk Management Department of the Group's holding company, working with the business operations worldwide, is responsible for arranging appropriate insurance coverage and organising Group wide risk reporting.

## Review of Internal Control Systems

The Board, through the Audit Committee, has conducted a review of the effectiveness of the Group's internal control systems for the year ended 31 December 2008, covering all material financial, operational and compliance controls and risk management functions.

## CODE OF ETHICS

The Group places utmost importance on employees' ethical, personal and professional standards. Every employee is provided with the Group's Code of Ethics booklet, and all employees are expected to adhere to the highest standards set out in the Code of Ethics.

## INVESTOR RELATIONS AND SHAREHOLDERS' RIGHTS

The Group actively promotes investor relations and communications with the investment community when the interim and year end financial results are announced and during the course of the year. Through its Chairman and Chief Executive Officer, the Group responds to requests for information and queries from the investment community including institutional shareholders, analysts and the media through regular briefing meetings, conference calls and presentations. The other Directors, including Non-executive Directors, develop an understanding of the views of the major shareholders about the Company by periodic meetings on the subject with the Chairman and the Chief Executive Officer.

The Board is committed to providing clear and full information on the Group to shareholders through the publication of notices, announcements, interim and annual reports. Moreover, additional information is also available to shareholders through the Investor Relations page on the Company's website.

Shareholders are encouraged to attend all general meetings of the Company, such as the annual general meeting for which at least 20 working days' notice is given and at which the Chairman and Directors are available to answer questions on the Group's businesses. All shareholders have statutory rights to call for extraordinary general meetings and put forward agenda items for consideration by shareholders by sending to the Company Secretary a written request for such general meetings together with the proposed agenda items. Financial and other information is made available on the Company's website, which is regularly updated.

The Group values feedback from shareholders on its efforts to promote transparency and foster investor relationships. Comments and suggestions are welcome and can be addressed to the Company Secretary by mail/email or by e-mail to the Company at info@chi-med.com.

By Order of the Board

**Edith Shih**
*Director and Company Secretary*

13 March 2009

# Independent Auditor's Report

## TO THE SHAREHOLDERS OF HUTCHISON CHINA MEDITECH LIMITED

*(incorporated in the Cayman Islands with limited liability)*

We have audited the consolidated accounts of Hutchison China MediTech Limited (the "Company") and its subsidiaries (together, the "Group") set out on pages 44 to 88, which comprise the consolidated balance sheet as of 31 December 2008, and the consolidated profit and loss account, the consolidated statement of changes in equity and the consolidated cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes.

## Directors' responsibility for the accounts

The directors of the Company are responsible for the preparation and fair presentation of these consolidated accounts in accordance with International Financial Reporting Standards. This responsibility includes designing, implementing and maintaining internal control relevant to the preparation and fair presentation of accounts that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

## Auditor's responsibility

Our responsibility is to express an opinion on these consolidated accounts based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance as to whether the accounts are free from material misstatement.

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

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

## Opinion

In our opinion, the consolidated accounts present fairly, in all material respects, the financial position of the Group as of 31 December 2008, and of the Group's financial performance and cash flows for the year then ended in accordance with International Financial Reporting Standards.

## Other matters

This report, including the opinion, has been prepared for and only for you, as a body, and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report.

**PricewaterhouseCoopers**
*Certified Public Accountants*

Hong Kong, 13 March 2009

# Consolidated Profit and Loss Account

*For the year ended 31 December 2008*

| | Note | 2008 US$'000 | 2007 US$'000 |
|---|---|---|---|
| **Continuing operations** | | | |
| Sales | 5 | **86,971** | 65,110 |
| Cost of sales | | **(36,127)** | (27,656) |
| Gross profit | | **50,844** | 37,454 |
| Selling expenses | | **(31,744)** | (23,091) |
| Administrative expenses | | **(35,086)** | (27,423) |
| Other net operating income | 6 | **1,759** | 3,337 |
| Operating loss | 7 | **(14,227)** | (9,723) |
| Finance costs | 8 | **(528)** | (299) |
| Loss before taxation | | **(14,755)** | (10,022) |
| Taxation charge | 9 | **(1,503)** | (838) |
| Loss for the year from continuing operations | | **(16,258)** | (10,860) |
| **Discontinued operations** | | | |
| Loss for the year from discontinued operations | 10 | **-** | (5,106) |
| Loss for the year | | **(16,258)** | (15,966) |
| Attributable to: | | | |
| Equity holders of the Company | | **(17,755)** | (17,191) |
| Minority interests | | **1,497** | 1,225 |
| | | **(16,258)** | (15,966) |
| Loss per share for loss from continuing operations attributable to equity holders of the Company for the year (US$ per share) | 11 | **(0.3466)** | (0.2360) |
| Loss per share for loss from continuing and discontinued operations attributable to equity holders of the Company for the year (US$ per share) | 11 | **(0.3466)** | (0.3357) |

# Consolidated Balance Sheet

*As at 31 December 2008*

| | Note | 2008 US$'000 | 2007 US$'000 |
|---|---|---|---|
| ASSETS | | | |
| Non-current assets | | | |
| Property, plant and equipment | 14 | **25,946** | 25,682 |
| Leasehold land | 15 | **6,082** | 5,828 |
| Goodwill | 16 | **7,052** | 6,616 |
| Trademarks and patents | 17 | **475** | 602 |
| Available-for-sale financial asset | 18 | **145** | 136 |
| Deferred tax assets | 19 | **333** | 256 |
| | | **40,033** | 39,120 |
| Current assets | | | |
| Inventories | 20 | **14,714** | 11,722 |
| Trade and bills receivables | 21 | **22,432** | 21,172 |
| Other receivables and prepayments | | **2,572** | 2,204 |
| Cash and bank balances | 22 | **38,206** | 53,345 |
| | | **77,924** | 88,443 |
| Total assets | | **117,957** | 127,563 |
| EQUITY | | | |
| Capital and reserves attributable to the Company's equity holders | | | |
| Share capital | 23 | **51,229** | 51,229 |
| Reserves | | **23,914** | 39,067 |
| | | **75,143** | 90,296 |
| Minority interests | | **9,283** | 7,311 |
| Total equity | | **84,426** | 97,607 |
| LIABILITIES | | | |
| Current liabilities | | | |
| Trade payables | 24 | **5,290** | 5,303 |
| Other payables and accruals | 25 | **18,836** | 17,042 |
| Amounts due to related parties | 30(b) | **974** | 496 |
| Current tax liabilities | | **536** | 551 |
| Short-term bank loans | 26 | **7,606** | 6,564 |
| | | **33,242** | 29,956 |
| Non-current liabilities | | | |
| Deferred tax liabilities | 19 | **289** | - |
| Total liabilities | | **33,531** | 29,956 |
| Total equity and liabilities | | **117,957** | 127,563 |

**Simon To**
*Director*

**Christian Hogg**
*Director*

# Consolidated Statement Of Changes In Equity

*For the year ended 31 December 2008*

| | Attributable to equity holders of the Company | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | Share capital US$'000 | Share premium US$'000 | Share-based compensation reserve US$'000 | Exchange reserve US$'000 | General reserves US$'000 | Accumulated losses US$'000 | Total US$'000 | Minority interests US$'000 | Total equity US$'000 |
| As at 1 January 2007 | 51,212 | 91,277 | 2,368 | 1,844 | 29 | (43,779) | 102,951 | 7,030 | 109,981 |
| Exchange translation differences | – | – | – | 2,037 | 1 | – | 2,038 | 333 | 2,371 |
| (Loss)/profit for the year | – | – | – | – | – | (17,191) | (17,191) | 1,225 | (15,966) |
| Issue of shares (Note 23 (a)) | 17 | 74 | (53) | – | – | – | 38 | – | 38 |
| Dividend paid to a minority shareholder of a subsidiary | – | – | – | – | – | – | – | (1,277) | (1,277) |
| Share-based compensation expenses | – | – | 2,460 | – | – | – | 2,460 | – | 2,460 |
| Transfer between reserves | – | – | (528) | – | 35 | 493 | – | – | – |
| As at 31 December 2007 | 51,229 | 91,351 | 4,247 | 3,881 | 65 | (60,477) | 90,296 | 7,311 | 97,607 |
| As at 1 January 2008 | **51,229** | **91,351** | **4,247** | **3,881** | **65** | **(60,477)** | **90,296** | **7,311** | **97,607** |
| Exchange translation differences | **-** | **-** | **-** | **1,647** | **-** | **-** | **1,647** | **475** | **2,122** |
| (Loss)/profit for the year | **-** | **-** | **-** | **-** | **-** | **(17,755)** | **(17,755)** | **1,497** | **(16,258)** |
| Share-based compensation expenses | **-** | **-** | **955** | **-** | **-** | **-** | **955** | **-** | **955** |
| Transfer between reserves | **-** | **-** | **(219)** | **-** | **-** | **219** | **-** | **-** | **-** |
| As at 31 December 2008 | **51,229** | **91,351** | **4,983** | **5,528** | **65** | **(78,013)** | **75,143** | **9,283** | **84,426** |

# Consolidated Cash Flow Statement

*For the year ended 31 December 2008*

| | Note | 2008 US$'000 | 2007 US$'000 |
|---|---|---|---|
| Cash flows from operating activities | | | |
| Net cash used in operations | 27 | **(12,433)** | (7,688) |
| Interest received | | **1,221** | 937 |
| Interest paid | | **(528)** | (367) |
| Income tax paid | | **(1,306)** | (543) |
| Net cash used in operating activities | | **(13,046)** | (7,661) |
| Cash flows from investing activities | | | |
| Purchase of property, plant and equipment | | **(3,397)** | (5,807) |
| Purchase of leasehold land | | **-** | (1,415) |
| Purchase of trademarks and patents | | **(1)** | (15) |
| Proceeds from disposal of property, plant and equipment | | **17** | - |
| Net cash used in investing activities | | **(3,381)** | (7,237) |
| Cash flows from financing activities | | | |
| Increase/(decrease) in amount due to immediate holding company | | **504** | (471) |
| Decrease in amount due to minority shareholders of a subsidiary | | **(40)** | - |
| Dividend paid to a minority shareholder of a subsidiary | | **-** | (1,277) |
| New short-term bank loans | | **2,110** | 4,760 |
| Repayment of short-term bank loans | | **(1,507)** | (5,709) |
| Issue of shares, net of share issuance costs | | **-** | 38 |
| Net cash generated from/(used in) financing activities | | **1,067** | (2,659) |
| Net decrease in cash and cash equivalents | | **(15,360)** | (17,557) |
| Cash and cash equivalents at 1 January | | **53,345** | 70,613 |
| Exchange differences | | **221** | 289 |
| Cash and cash equivalents at 31 December | | **38,206** | 53,345 |
| Analysis of cash and cash equivalents | | | |
| – Cash and bank balances | 22 | **38,206** | 53,345 |

# Notes To The Accounts

## 1 GENERAL INFORMATION

Hutchison China MediTech Limited (the "Company") and its subsidiaries (together the "Group") is principally engaged in the manufacturing, distribution and sales of traditional Chinese medicine ("TCM") and healthcare products. The Group is also engaged in carrying out pharmaceutical research and development. The Group and its jointly controlled entities have manufacturing plants in Shanghai and Guangzhou in the Peoples' Republic of China (the "PRC") and sell mainly in the PRC, United Kingdom ("UK") and France.

The Company was incorporated in the Cayman Islands on 18 December 2000 as an exempted company with limited liability under the Companies Law (2000 Revision), Chapter 22 of the Cayman Islands. The address of its registered office is P.O Box 309, Ugland House, Grand Cayman, KY1-1104, Cayman Islands.

The Company's ordinary shares were admitted to trading on the Alternative Investment Market operated by the London Stock Exchange ("AIM"). These consolidated accounts are presented in thousands of United States Dollars ("US$'000"), unless otherwise stated.

## 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The consolidated accounts of the Company have been prepared in accordance with International Financial Reporting Standards ("IFRS"). These consolidated accounts have been prepared under the historical cost convention except that certain financial assets and liabilities are measured at fair values, as appropriate.

### (a) Basis of consolidation

The consolidated accounts of the Group include the accounts of the Company and all its direct and indirect subsidiaries made up to 31 December and also incorporate the Group's interests in jointly controlled entities on the basis set out in Note 2(c) below.

All significant intercompany transactions and balances within the Group are eliminated on consolidation.

Minority interests represent the interests of outside shareholders in the operating results and net assets of subsidiaries and subsidiaries of jointly controlled entities.

### (b) Subsidiaries

A subsidiary is an entity that the Company has the power, directly or indirectly, to govern the financial and operating policies, so as to obtain benefits from their activities.

Subsidiaries are fully consolidated from the date on which control is transferred to the Group. They are de-consolidated from the date that control ceases.

### (c) Jointly controlled entities

Jointly controlled entities are joint ventures in respect of which a contractual arrangement is established between the participating venturers and whereby the Group together with the other venturers undertake an economic activity which is subject to joint control and none of the venturers has unilateral control over the economic activity.

The Group's interests in jointly controlled entities are accounted for by proportionate consolidation. Under this method, the Group combines its share of the joint ventures' individual income and expenses, assets and liabilities and cash flows on a line-by-line basis with similar items in the Group's consolidated accounts from the date that joint control commences until the date that joint control ceases.

The Group recognises the portion of gains or losses on the sale of assets by the Group to the jointly controlled entities that is attributable to the other venturers. The Group does not recognise its share of profits or losses from the jointly controlled entities that result from the Group's purchase of assets from the jointly controlled entities until it resells the assets to an independent party. However, a loss on the transaction is recognised immediately if the loss provides evidence of a reduction in the net realisable value of current assets, or an impairment loss.

## 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### (d) Foreign currency translation

Items included in the accounts of each of the Group's companies are measured using the currency of the primary economic environment in which the entity operates (the "functional currency"). The functional currency of the Company and most of its principal subsidiaries and jointly controlled entities is Renminbi ("RMB") whereas the consolidated accounts are presented in United States Dollars ("US dollars"), which is the Company's presentation currency , as the Company holds investments in various countries and US dollars is considered as a common currency.

Transactions in foreign currencies are converted at the rates of exchange ruling at the transaction dates. Monetary assets and liabilities are translated at the rates of exchange ruling at the balance sheet date. Exchange differences are included in the determination of profit or loss.

The accounts of overseas subsidiaries and jointly controlled entities are translated into the Company's presentation currency using the year end rates of exchange for the balance sheet items and the average rates of exchange for the year for the profit and loss account items. Exchange differences are dealt with as a movement in exchange reserve.

### (e) Property, plant and equipment

Property, plant and equipment other than construction in progress are stated at historical cost less accumulated depreciation and accumulated impairment losses. Historical cost includes the purchase price of the asset and any directly attributable costs of bringing the asset to its working condition and location for its intended use.

Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. All other repairs and maintenance are charged to the profit and loss account during the financial period in which they are incurred.

Depreciation is calculated using the straight-line method to allocate their costs less accumulated impairment losses over their estimated useful lives. The principal annual rates are as follows:

| | |
|---|---|
| Buildings | 20-30 years |
| Leasehold improvements | Over the unexpired period of the lease or 3-5 years, whichever is shorter |
| Plant and equipment | 10 years |
| Furniture and fixtures, other equipment and motor vehicles | 4-5 years |

The assets' useful lives are reviewed, and adjusted if appropriate, at each balance sheet date. An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount (Note 2(k)).

Gains or losses on disposals are determined by comparing net sales proceeds with the carrying amount of the relevant assets and are recognised in profit or loss.

## 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### (f) Construction-in-progress

Construction-in-progress represents buildings, plant and machinery under construction and pending installation and is stated at cost less accumulated impairment losses (if any). Cost includes the costs of construction of buildings and the costs of plant and machinery. No provision for depreciation is made on construction-in-progress until such time as the relevant assets are completed and ready for intended use. When the assets concerned are brought into use, the costs are transferred to property, plant and equipment and depreciated in accordance with the policy as stated in Note 2(e).

### (g) Leasehold land

Leasehold land is stated at cost less accumulated amortisation and accumulated impairment losses (if any). Cost mainly represents consideration paid for the rights to use the land on which various plants and buildings are situated for a period of 50 years from the date the respective right was granted. Amortisation of leasehold land is calculated on a straight-line basis over the period of the land use rights.

### (h) Goodwill

Goodwill represents the excess of the cost of an acquisition over the fair value of the Group's share of the net identifiable assets of the acquired subsidiary or jointly controlled entity at the date of acquisition. Goodwill on acquisition of a foreign operation is treated as an asset of the foreign operation.

Goodwill arising on acquisition is retained at the carrying amount as a separate asset, and subject to impairment test annually and when there are indications that the carrying value may not be recoverable. If the cost of acquisition is less than the fair value of the Group's share of the net identifiable assets of the acquired subsidiary or jointly controlled entity, the difference is recognised directly in the consolidated profit and loss account.

The profit or loss on disposal of a subsidiary or jointly controlled entity is calculated by reference to the net assets at the date of disposal including the attributable amount of goodwill but does not include any attributable goodwill previously eliminated against reserves.

### (i) Trademarks and patents

Trademarks and patents have definite useful lives and are carried at historical cost less accumulated amortisation and accumulated impairment losses. Amortisation is calculated using the straight-line method to allocate the costs of trademarks and patents over their estimated useful lives of ten years.

### (j) Research and development

Research expenditure is recognised as an expense as incurred. Costs incurred on development projects (relating to the design and testing of new or improved products) are recognised as intangible assets when it is probable that the project will be a success considering its commercial and technological feasibility, and costs can be measured reliably. Other development expenditures are recognised as an expense as incurred. Development costs previously recognised as an expense are not recognised as an asset in a subsequent period. Development costs with a finite useful life that have been capitalised (if any) are amortised from the commencement of the commercial production of the product on a straight-line basis over the period of expected benefit, not exceeding five years.

Where the research phase and the development phase of an internal project cannot be clearly distinguished, all expenditure incurred on the project is charged to the profit and loss account.

## 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### (k) Impairment of assets

Assets that have an indefinite useful life are tested for impairment annually. Assets are reviewed for impairment to determine whether there is any indication that the carrying value of these assets may not be recoverable and have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss, if any. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. Such impairment loss is recognised in the profit and loss account.

### (l) Available-for-sale financial assets

Available-for-sale financial assets are non-derivatives that are either designated in this category or not classified as loans and receivables, held-to-maturity investments or financial assets at fair value through profit or loss. These investments are initially recognised in the balance sheet at fair value plus transaction costs and measured at each subsequent reporting date at fair value, except for equity investments that do not have a quoted market price in an active market and whose fair value cannot be reliably measured, they are measured at cost less impairment losses. Changes in fair value are dealt with as movements in reserve except for impairment losses which are charged to the profit and loss account. Where these investments are interest-bearing, interest calculated using the effective interest method is recognised in profit or loss. Dividends from available-for-sale financial assets are recognised when the right to receive payment is established. When available-for-sale financial assets are sold, the cumulative fair value gains or losses previously recognised in reserve is recognised in the profit and loss account.

### (m) Inventories

Inventories are stated at the lower of cost and net realisable value. Cost is determined using the weighted average cost method. The cost of finished goods and work in progress comprises raw materials, direct labor, other direct costs and related production overheads (based on normal operating capacity). Net realisable value is the estimated selling price in the ordinary course of business, less applicable variable selling expenses.

### (n) Trade and other receivables

Trade and other receivables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method, less provision for impairment. A provision for impairment of trade receivables is established when there is objective evidence that the asset is impaired. The amount of the provision is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the effective interest rate. The amount of the provision is recognised in the profit and loss account.

### (o) Cash and cash equivalents

Cash and cash equivalents comprise cash on hand and demand deposits.

### (p) Borrowings

Borrowings are recognised initially at fair value, net of transaction costs incurred. Borrowings are subsequently stated at amortised cost; any difference between the proceeds (net of transaction costs) and the redemption value is recognised in profit or loss over the period of the borrowings using the effective interest method.

## 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### (q) Financial liabilities

Financial liabilities (including trade and other payables) are initially recognised at fair value and subsequently measured at amortised cost using the effective interest method.

### (r) Deferred income tax

Deferred income tax is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated accounts. Deferred income tax assets are recognised to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised.

### (s) Employee benefits

#### *(i) Pension plans*

The Group operates various defined contribution plans. The Group's contributions to the defined contribution plans are charged to the profit and loss account in the year incurred.

Pension costs are charged against the profit and loss account within staff costs.

The pension plans are generally funded by the relevant group companies and by payments from employees of the contributory plans.

#### *(ii) Share-based payments*

The Group operates certain share-based compensation plans. The fair value of the employee services received in exchange for the grant of the options is recognised as an expense. The total amount to be expensed over the vesting period is determined by reference to the fair value of the options granted, excluding the impact of any non-market vesting conditions (for example, profitability and sales growth targets). Non-market vesting conditions are included in assumptions about the number of options that are expected to vest. At each balance sheet date, the Group revises its estimates of the number of options that are expected to vest. It recognises the impact of the revision of original estimates, if any, in profit or loss, with a corresponding adjustment to equity.

The proceeds received net of any directly attributable transaction costs are credited to share capital (nominal value) and share premium when the options are exercised. When the share options are forfeited after the vesting date or are still not exercised at the expiry date, the amount previously recognised in the share-based compensation reserve will be transferred to retained profits.

### (t) Provisions

Provisions are recognised when the Group has a present legal or constructive obligation as a result of past events; it is probable that an outflow of resources will be required to settle the obligation; and the amount has been reliably estimated. Provisions are not recognised for future operating losses.

## 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### (u) Operating leases

Leases in which a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. Payments made under operating leases are charged to the profit and loss account on a straight-line basis over the period of the lease.

### (v) Borrowing costs

Borrowing costs directly attributable to the acquisition, construction or production of qualifying assets, which are assets that necessarily take a substantial period of time to get ready for their intended use or sale, are added to the cost of those assets, until such time as the assets are substantially ready for their intended use or sale. All other borrowing costs are recognised in the profit and loss account in the period in which they are incurred.

### (w) Government incentives

Incentives from government are recognised at their fair values where there is a reasonable assurance that the incentives will be received and all attached conditions will be complied with. Government incentives relating to costs are deferred and recognised in the profit and loss account over the period necessary to match them with the costs that they are intended to compensate.

### (x) Revenue and income recognition

Revenue comprises the fair value of the consideration received and receivable for the sales of goods and services in the ordinary course of the Group's activities. Revenue is shown net of value-added tax, returns, volume rebates and discounts after eliminated sales within the Group. Revenue and income are recognised as follows:

#### *(i) Sales of goods - wholesales*

Sales of goods are recognised when a group entity has delivered products to the customer, the customer has accepted the products and collectibility of the related receivables is reasonably assured.

#### *(ii) Sales of goods - retail*

Sales of goods are recognised at point of sales less an estimate for sales return based on past experience where goods are sold with a right to return. Retail sales are usually in cash or by credit card. The recorded revenue is the gross amount of sales, including credit card fees payable for the transaction. Such fees are included in selling expenses.

#### *(iii) Service income*

Revenue from the provision of pharmaceutical research and development services, and consultation and treatments services is recognised when services are rendered.

#### *(iv) Interest income*

Interest income is recognised on a time-proportion basis using the effective interest method.

## 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

At the date of authorisation of these consolidated accounts, the following standards, amendments and interpretations were in issue but not yet effective:

| | |
|---|---|
| IAS 1 (Revised) | Presentation of Financial Statements |
| IAS 23 (Revised) | Borrowing Costs |
| IAS 27 (Revised) | Consolidated and Separate Financial Statements |
| IAS 32 (Amendment) and IAS 1 (Amendment) | Puttable Financial Instruments and Obligations Arising on Liquidation |
| IAS 39 (Amendment) | Eligible Hedge Items |
| IFRS 1 and IAS 27 (Amendments) | First Time Adoption of IFRS and Consolidated and Separate Financial Statements |
| IFRS 2 (Amendment) | Share-based Payment Vesting Conditions and Cancellations |
| IFRS 3 (Revised) | Business Combination |
| IFRS 8 | Operating Segments |
| IFRIC 13 | Customer Loyalty Programmes |
| IFRIC 15 | Agreements for the Construction of Real Estate |
| IFRIC 16 | Hedges of a Net Investment in a Foreign Operation |
| IFRIC 17 | Distributions of Non-cash Assets |
| IFRIC 18 | Transfers of Assets from Customers |

The effect that the adoption of IFRS 3 (Revised), IAS 27 (Revised) and IFRIC 17 will have on the results and financial position of the Group will depend on the incidence and timing of transactions within the scope of these standards and interpretation occurring on or after 1 January 2010.

The adoption of other standards, amendments and interpretations listed above in future periods is not expected to result in substantial changes to the Group's accounting policies.

In addition, International Accounting Standard Board also published a number of amendments to the existing standards under its annual improvement project. These amendments are not expected to have a significant financial impact on the results and financial position of the Group.

## 3 FINANCIAL RISK MANAGEMENT

### (a) Financial risk factors

The Group's activities expose it to a variety of financial risks, including foreign exchange risk, credit risk, cash flow interest rate risk and liquidity risk. The Group does not use any derivative financial instruments for the year.

#### *(i) Foreign exchange risk*

The Group mainly operates in the PRC with most of the transactions settled in RMB. The Group also has retail operations in the UK. The Group's assets and liabilities, and transactions arising from its operations that are exposed to foreign exchange risk are primarily with respect to the US Dollars and UK pound sterling.

Management has a policy to require group companies to manage their foreign exchange risk against functional currency. It mainly includes managing the exposures arise from sales and purchases made by the relevant group companies in currencies other than their own functional currencies. The Group also manages its foreign exchange risk by performing regular reviews of the Group's net foreign exchange exposures. The Group has not used any hedging arrangement to hedge its exposure during the year as foreign currency risk is considered insignificant.

As the assets and liabilities of each company within the Group are mainly denominated in the respective company's functional currency, management considers that the Group's volatility against changes in exchange rates of foreign currencies would not be significant. Accordingly, no sensitivity analysis is presented for foreign exchange risk.

#### *(ii) Credit risk*

The carrying amounts of cash and cash equivalents, trade and bills receivables and other receivables included in the consolidated balance sheet represent the Group's maximum exposure to credit risk of the counterparty in relation to its financial assets.

Substantially all of the Group's cash and cash equivalents are deposited in major financial institutions located in Hong Kong and the PRC, which management believes are of high credit quality. The Group has a policy to limit the amount of credit exposure to any financial institution.

The Group has no significant concentrations of credit risk. The Group has policies in place to ensure that wholesales of products are made to customers with an appropriate credit history and the Group performs periodic credit evaluations of its customers. Normally the Group does not require collaterals from trade debtors. Sales to retail customers are made in cash or via major credit cards.

Management makes periodic assessment on the recoverability of trade and bills receivables and other receivables. The Group's historical experience in collection of these receivables falls within the recorded allowances.

#### *(iii) Cash flow interest rate risk*

The Group has no significant interest-bearing assets except for the cash at bank and bank deposits. The Group's exposure to changes in interest rates is mainly attributable to its short-term borrowings, which expose the Group to cash flow interest rate risk. The Group has not used any interest rate swaps to hedge its exposure to interest rate risk as management considers that the Group's short-term borrowings are relatively insignificant to the Group; any reasonable changes in interest rate would not result in a significant change in the Group's results. Accordingly, no sensitivity analysis is presented for cash flow interest rate risk.

## 3 FINANCIAL RISK MANAGEMENT (Continued)

### (a) Financial risk factors (Continued)

#### *(iv) Liquidity risk*

Prudent liquidity management implies maintaining sufficient cash and cash equivalents and the availability of funding when necessary. The Group's policy is to regularly monitor current and expected liquidity requirements to ensure that it maintains sufficient cash balances and adequate credit facilities to meet its liquidity requirements in the short and long term.

The Group's primary cash requirements have been for additions of and upgrades on property, plant and equipment, settlement of short-term bank loans, settlement of payables and payment for operating expenses. The Group mainly finances its working capital requirements through a combination of internal resources and bank borrowings.

As at 31 December 2007 and 2008, all of the Group's financial liabilities were due for settlement contractually within 12 months.

### (b) Capital risk management

The Group's objectives when managing capital are to safeguard the Group's ability to provide returns for shareholders and benefits for other stakeholders and to maintain an optimal capital structure to reduce the cost of capital.

The Group regularly reviews and manages its capital structure to ensure optimal capital structure to maintain a balance between higher shareholders' return that might be possible with higher levels of borrowings and advantages and security afforded by a sound capital position, and makes adjustments to the capital structure in light of changes in economic conditions.

The Group monitors capital on the basis of the gearing ratio. This ratio is calculated as total borrowings divided by total equity attributable to the Company's equity holders as shown on the consolidated balance sheet. Total borrowings include current borrowings and non-current borrowings, if any.

Currently, it is the Group's strategy to maintain a minimal use of borrowings. The gearing ratios as at 31 December 2008 and 2007 were as follows:

| | **2008**<br>**US$'000** | 2007<br>US$'000 |
|---|---|---|
| Total borrowings (Note 26) | **7,606** | 6,564 |
| Total equity attributable to the Company's equity holders | **75,143** | 90,296 |
| Gearing ratio | **10.1%** | 7.3% |

The increase in the gearing ratio during 2008 resulted primarily from the operating loss incurred for the year.

## 3 FINANCIAL RISK MANAGEMENT (Continued)

### (c) Fair value estimation

The carrying amounts of the Group's current financial assets, including cash and bank balances, trade and bills receivables, and other receivables, and current financial liabilities, including trade payables, other payables and accruals, short-term borrowings, and balances with related parties, approximate their fair values due to their short term maturities.

The face values less any estimated credit adjustments for financial assets and liabilities with a maturity of less than one year are assumed to approximate their fair values. The fair value of financial liabilities for disclosure purposes is estimated by discounting the future contractual cash flows at the current market interest rate that is available to the Group for similar financial instruments.

## 4 CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS

Note 2 includes a summary of the significant accounting policies used in the preparation of the accounts. The preparation of accounts often requires the use of judgements to select specific accounting methods and policies from several acceptable alternatives. Furthermore, significant estimates and assumptions concerning the future may be required in selecting and applying those methods and policies in the accounts. The Group bases its estimates and judgements on historical experience and various other assumptions that it believes are reasonable under the circumstances. Actual results may differ from these estimates and judgements under different assumptions or conditions.

The following is a review of the more significant assumptions and estimates, as well as the accounting policies and methods used in the preparation of the accounts.

### (a) Useful lives of property, plant and equipment

The Group has made substantial investments in property, plant and equipment. Changes in technology or changes in the intended use of these assets may cause the estimated period of use or value of these assets to change.

### (b) Impairment of assets

The Group tests annually whether goodwill has suffered any impairment. Other assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of the asset exceeds its recoverable amount in accordance with the accounting policy stated in Note 2(k). The recoverable amount of an asset or a cash-generating unit is determined based on the higher of the asset's or the cash-generating unit's fair value less costs to sell and value-in-use. The value-in-use calculation requires the entity to estimate the future cash flows expected to arise from the asset and a suitable discount rate in order to calculate present value, which has been prepared on the basis of management's assumptions and estimates.

### (c) Impairment of receivables

The Group makes provision for impairment of receivables based on an assessment of the recoverability of the receivables. This assessment is based on the credit history of the relevant counterparty and the current market condition. Provisions are made where events or changes in circumstances indicate that the receivables may not be collectible. The identification of impairment in receivables requires the use of judgement and estimates. Where the expectation is different from the original estimate, such difference will impact the carrying amount of receivables and impairment is recognised in the period in which such estimate has been changed.

## 4 CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS (Continued)

### (d) Research and development costs

Research expenditure is recognised as an expense as incurred. Where the research phase and the development phase of an internal project cannot be clearly distinguished, all expenditure incurred on the project is charged to the profit and loss account. In determining whether the development costs can be capitalised, management assesses the probability that the project will be a success by considering its commercial and technical feasibility. This assessment could change when there are subsequent technological advancement and innovations.

### (e) Deferred income tax

The Group has significant tax losses carried forward and has not recognised the deferred income tax assets on these losses. Deferred income tax assets in respect of tax losses are recognised to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised. No deferred income tax assets are recognised when it is uncertain whether there are sufficient future taxable profits available before such tax losses expire. Where the final outcome of these uncertainties are different from the estimation, such differences will impact the carrying amount of deferred tax assets in the period in which such determination is made.

## 5 REVENUE AND SEGMENT INFORMATION

The Group is principally engaged in the manufacturing, distribution and sales of TCM and healthcare products. Revenue recognised for the year are as follows:

| | **2008**<br>**US$'000** | 2007<br>US$'000 |
|---|---|---|
| Continuing operations | | |
| Sales of goods | **82,173** | 62,530 |
| Services income | **4,798** | 2,580 |
| | **86,971** | 65,110 |
| Discontinued operations | | |
| Sales of goods | **-** | 4,551 |
| | **86,971** | 69,661 |

### Primary reporting format – business segments

The Group's activities are categorised into four main areas:

- China healthcare – Health supplement: comprises the research and development, manufacture, distribution and sale of western and TCM health supplements products.
- China healthcare – Over-the-counter ("OTC") & prescription: comprises the development, manufacture, distribution and sale of OTC & prescription TCM products.
- Consumer products: relates to TCM pharmaceuticals and sales of TCM-based consumer lifestyle products and services.
- Drug research and development: relates mainly to drug discoveries and other pharmaceutical research and development activities, and the provision of research and development services.

## 5 REVENUE AND SEGMENT INFORMATION (Continued)

### Primary reporting format – business segments (Continued)

In December 2007, the Group discontinued its operations in respect of the Nao Ling Tong memory supplement ("NLT") operation, which was a component of the Group included in the China healthcare – Health supplement business segment. Details of the discontinued operations are included in Note 10.

*Continuing operations*

| | As at and for the year ended 31 December 2008 | | | | | |
|---|---|---|---|---|---|---|
| | China healthcare - Health supplement US$'000 | China healthcare - OTC & prescription US$'000 | Consumer products US$'000 | Drug research and development US$'000 | Unallocated (Note a) US$'000 | Total US$'000 |
| Sales | 5,526 | 75,144 | 4,051 | 2,250 | - | 86,971 |
| Segment results | 270 | 8,869 | (2,604) | (15,403) | (5,359) | (14,227) |
| Finance costs | | | | | | (528) |
| Loss before taxation | | | | | | (14,755) |
| Taxation charge | | | | | | (1,503) |
| Loss for the year | | | | | | (16,258) |
| Segment assets (Note b) | 3,382 | 71,320 | 3,568 | 8,722 | 30,965 | 117,957 |
| Segment liabilities (Note c) | 2,172 | 15,503 | 428 | 4,966 | 10,216 | 33,285 |
| Other segment items | | | | | | |
| Capital expenditure (Notes 14, 15 and 17) | 20 | 837 | 1,035 | 1,493 | 13 | 3,398 |
| Depreciation (Note 7) | 18 | 2,279 | 494 | 1,519 | 21 | 4,331 |
| Amortisation (Notes 15 and 17) | - | 281 | - | 40 | - | 321 |
| Provision for trade receivables | - | 11 | - | - | - | 11 |
| Provision for inventories | - | - | 6 | - | - | 6 |

## 5 REVENUE AND SEGMENT INFORMATION (Continued)

### Primary reporting format – business segments (Continued)

*Discontinued operations*

| | As at and for the year ended 31 December 2008 | | | | | |
|---|---|---|---|---|---|---|
| | China healthcare - Health supplement US$'000 | China healthcare - OTC & prescription US$'000 | Consumer products US$'000 | Drug research and development US$'000 | Unallocated US$'000 | Total US$'000 |
| Sales | – | – | – | – | – | – |
| Segment results | – | – | – | – | – | – |
| Finance costs | | | | | | – |
| Loss before taxation | | | | | | – |
| Taxation charge | | | | | | – |
| Loss for the year | | | | | | – |
| Segment assets | – | – | – | – | – | – |
| Segment liabilities | 246 | – | – | – | – | 246 |
| Other segment items | | | | | | |
| Capital expenditure, depreciation, amortisation, provisions for trade and other receivables, and inventories | – | – | – | – | – | – |

## 5 REVENUE AND SEGMENT INFORMATION (Continued)

### Primary reporting format – business segments (Continued)

*Continuing operations*

| | As at and for the year ended 31 December 2007 | | | | | |
|---|---|---|---|---|---|---|
| | China healthcare – Health supplement US$'000 | China healthcare – OTC & prescription US$'000 | Consumer products US$'000 | Drug research and development US$'000 | Unallocated (Note a) US$'000 | Total US$'000 |
| Sales | 3,719 | 57,648 | 2,865 | 878 | – | 65,110 |
| Segment results | 222 | 6,597 | (2,143) | (10,106) | (4,293) | (9,723) |
| Finance costs | | | | | | (299) |
| Loss before taxation | | | | | | (10,022) |
| Taxation charge | | | | | | (838) |
| Loss for the year | | | | | | (10,860) |
| Segment assets (Note b) | 2,875 | 61,266 | 3,334 | 7,563 | 52,525 | 127,563 |
| Segment liabilities (Note c) | 2,588 | 15,254 | 441 | 3,218 | 7,937 | 29,438 |
| Other segment items | | | | | | |
| Capital expenditure (Notes 14, 15 and 17) | 22 | 1,313 | 400 | 5,469 | 33 | 7,237 |
| Depreciation (Note 7) | 4 | 1,778 | 582 | 983 | 15 | 3,362 |
| Amortisation (Notes 15 and 17) | – | 297 | – | 26 | – | 323 |
| Provision for trade receivables | – | 5 | – | – | – | 5 |
| Provision for inventories | – | – | – | – | – | – |

## 5 REVENUE AND SEGMENT INFORMATION (Continued)

### Primary reporting format – business segments (Continued)

*Discontinued operations*

| | As at and for the year ended 31 December 2007 | | | | | |
|---|---|---|---|---|---|---|
| | China healthcare – Health supplement US$'000 | China healthcare – OTC & prescription US$'000 | Consumer products US$'000 | Drug research and development US$'000 | Unallocated US$'000 | Total US$'000 |
| Sales | 4,551 | – | – | – | – | 4,551 |
| Segment results | (5,038) | – | – | – | – | (5,038) |
| Finance costs | | | | | | (68) |
| Loss before taxation | | | | | | (5,106) |
| Taxation charge | | | | | | – |
| Loss for the year | | | | | | (5,106) |
| Segment assets | – | – | – | – | – | – |
| Segment liabilities | 518 | – | – | – | – | 518 |
| Other segment items | | | | | | |
| Capital expenditure | – | – | – | – | – | – |
| Depreciation (Note 10) | 115 | – | – | – | – | 115 |
| Amortisation | – | – | – | – | – | – |
| Provisions for trade and other receivables | 1,729 | – | – | – | – | 1,729 |
| Provision for inventories | 326 | – | – | – | – | 326 |

Note:

(a) Unallocated expenses mainly represent corporate expenses which include corporate employee benefits expense and the relevant share-based compensation expenses.

(b) Segment assets mainly comprise property, plant and equipment, leasehold land, goodwill, inventories, trade and bills receivables and other receivables. Unallocated assets mainly comprise short-term corporate bank deposits.

(c) Segment liabilities mainly comprise trade payables, other payables and accruals. Unallocated liabilities mainly comprise accruals for corporate expenses, short-term bank loans, current and deferred tax liabilities and amount due to immediate holding company.

## 5 REVENUE AND SEGMENT INFORMATION (Continued)

### Secondary reporting format - geographical segments

*Continuing operations*

| | As at and for the year ended 31 December 2008 | | | | |
|---|---|---|---|---|---|
| | PRC US$'000 | UK US$'000 | France US$'000 | Unallocated US$'000 | Total US$'000 |
| Sales | 82,920 | 3,747 | 304 | - | 86,971 |
| Segment results | (6,264) | (1,841) | (763) | (5,359) | (14,227) |
| Segment assets | 83,424 | 3,254 | 314 | 30,965 | 117,957 |
| Capital expenditure (Notes 14, 15 and 17) | 2,350 | 1,032 | 3 | 13 | 3,398 |

*Discontinued operations*

| | As at and for the year ended 31 December 2008 | | | | |
|---|---|---|---|---|---|
| | PRC US$'000 | UK US$'000 | France US$'000 | Unallocated US$'000 | Total US$'000 |
| Sales, segment results, segment assets and capital expenditure | - | - | - | - | - |

## 5 REVENUE AND SEGMENT INFORMATION (Continued)

### Secondary reporting format – geographical segments (Continued)

*Continuing operations*

| | As at and for the year ended 31 December 2007 | | | | |
|---|---|---|---|---|---|
| | PRC US$'000 | UK US$'000 | France US$'000 | Unallocated US$'000 | Total US$'000 |
| Sales | 62,245 | 2,865 | – | – | 65,110 |
| Segment results | (3,287) | (2,143) | – | (4,293) | (9,723) |
| Segment assets | 71,704 | 3,334 | – | 52,525 | 127,563 |
| Capital expenditure (Notes 14, 15 and 17) | 6,804 | 400 | – | 33 | 7,237 |

*Discontinued operations*

| | As at and for the year ended 31 December 2007 | | | | |
|---|---|---|---|---|---|
| | PRC US$'000 | UK US$'000 | France US$'000 | Unallocated US$'000 | Total US$'000 |
| Sales | 4,551 | – | – | – | 4,551 |
| Segment results | (5,038) | – | – | – | (5,038) |
| Segment assets and capital expenditure | – | – | – | – | – |

## 6 OTHER NET OPERATING INCOME

| | 2008 US$'000 | 2007 US$'000 |
|---|---|---|
| Interest income | 1,221 | 937 |
| Fair value gain on financial assets at fair value through profit or loss | - | 1,657 |
| Net foreign exchange gains | 17 | 500 |
| Government incentives | 96 | - |
| Other operating income | 493 | 321 |
| Other operating expenses | (68) | (94) |
| | 1,759 | 3,321 |
| Attributable to: | | |
| Continuing operations | 1,759 | 3,337 |
| Discontinued operations | - | (16) |
| | 1,759 | 3,321 |

## 7 OPERATING LOSS

Operating loss is stated after charging the following:

| | 2008 US$'000 | 2007 US$'000 |
|---|---|---|
| Auditors' remuneration | 428 | 347 |
| Amortisation of trademarks and patents recognised in administrative expenses (Note 17) | 191 | 212 |
| Amortisation of leasehold land (Note 15) | 130 | 111 |
| Cost of inventories recognised as expense | 32,641 | 26,945 |
| Depreciation on property, plant and equipment – continuing operations | 4,331 | 3,362 |
| Write-off of inventories – continuing operations | 225 | 359 |
| Provision for inventories – continuing operations | 6 | - |
| Provision for trade receivables – continuing operations | 11 | 5 |
| Impairment of property, plant and equipment – continuing operations | - | 50 |
| Loss on disposal of property, plant and equipment | 110 | 269 |
| Operating lease rentals in respect of land and buildings | 1,907 | 1,409 |
| Research and development expense | 8,808 | 5,643 |
| Employee benefits expense (Note 13) | 19,252 | 16,092 |

## 8 FINANCE COSTS

| | 2008 US$'000 | 2007 US$'000 |
|---|---|---|
| Interest expense on short-term bank loans | 528 | 367 |
| Attributable to: | | |
| Continuing operations | 528 | 299 |
| Discontinued operations | - | 68 |
| | 528 | 367 |

## 9 TAXATION CHARGE

| | 2008 US$'000 | 2007 US$'000 |
|---|---|---|
| Continuing operations: | | |
| Current tax | 1,291 | 1,094 |
| Deferred income tax (Note 19) | 212 | (256) |
| Taxation charge | 1,503 | 838 |

(a) The Group has no estimated assessable profit in Hong Kong, UK and France for the year (2007: Nil).

(b) Pursuant to the relevant PRC enterprise income tax rules and regulations, a special income tax rate of 15% (2007: 15%) has been granted to Hutchison MediPharma Limited, a subsidiary of the Group, as a foreign invested enterprise which is engaged in research and development activities. The company will be subject to tax rates gradually increased to 25% towards year 2012.

Hutchison Healthcare Limited, a subsidiary of the Group, is entitled to a two-year exemption from income taxes followed by a 50% reduction in income taxes for the ensuing three years. These tax benefits will be expiring towards year 2012 and thereafter the company will be subject to a tax rate of 25%.

In addition, Hutchison Whampoa Guangzhou Baiyunshan Chinese Medicine Company Limited ("HBYS") and Shanghai Hutchison Pharmaceuticals Limited ("SHPL"), jointly controlled entities of the Group, continue to enjoy a 50% reduction in income taxes at a rate of 12.5% for the years ended 2008 and 2009. During the year ended 31 December 2008, both HBYS and SHPL have been granted High and New Technology Enterprise status and accordingly will be subject to a preferential income tax rate of 15% for the year 2010. These companies will be subject to a tax rate of 25% thereafter.

## 9 TAXATION CHARGE (Continued)

(c) The taxation charge on the Group's loss before taxation differs from the theoretical amount that would arise using the Group's weighted average tax rate as follows:

| | 2008 US$'000 | 2007 US$'000 |
|---|---|---|
| Loss before taxation | | |
| – Continuing operations | **(14,755)** | (10,022) |
| – Discontinued operations | **-** | (5,106) |
| | **(14,755)** | (15,128) |
| Tax calculated at the domestic tax rates of respective companies | **(2,341)** | (2,590) |
| Effect of tax concession | **(194)** | (276) |
| Expenses not deductible for tax purposes | **434** | 620 |
| Utilisation of previously unrecognised tax losses | **(8)** | (20) |
| Tax losses for which no deferred tax asset was recognised | **3,372** | 3,132 |
| Others | **240** | (28) |
| Taxation charge | **1,503** | 838 |

The weighted average applicable tax rate for the year was 15.9% (2007: 17.1%). The fluctuation in the weighted average applicable tax rate arose because of the changes in the relative profitability of the Group's operations in different tax jurisdictions.

# Notes To The Accounts

## 10 RESULTS AND CASH FLOWS OF DISCONTINUED OPERATIONS

In December 2007, the Group discontinued its NLT operations, which represented a separate major line of the Group's business, as the product line performed below expectation in light of increased competitive and regulatory activities in the generic health supplement market.

The results and cash flows of the discontinued operations are set out below.

| | 2008 US$'000 | 2007 US$'000 |
|---|---|---|
| Revenue | - | 4,551 |
| Expenses (note (a)) | - | (9,657) |
| Loss before taxation from discontinued operations | - | (5,106) |
| Taxation charge | - | – |
| Loss for the year from discontinued operations (note (b)) | - | (5,106) |
| Cash flows from discontinued operations | | |
| Net cash flows from operating activities | - | (2,194) |
| Net cash flows from investing activities | - | (14) |
| Net cash flows from financing activities | - | (174) |
| Net cash flows | - | (2,382) |
| (a) Expenses include: | | |
| Depreciation on property, plant and equipment | - | 115 |
| Provision for inventories | - | 326 |
| Provision for trade and other receivables | - | 1,729 |
| Impairment of property, plant and equipment | - | 553 |

(b) Included in the loss from discontinued operations of US$5,106,000 for the year 2007 was a loss on measurement to fair value less costs to sell of US$2,608,000, and related tax expense of US$Nil.

## 11 LOSS PER SHARE

Basic loss per share is calculated by dividing the loss attributable to equity holders of the Company by the weighted average number of ordinary shares in issue during the year.

| | 2008 | 2007 |
|---|---|---|
| Loss for the year | | |
| – Continuing operations (US$'000) | (17,755) | (12,085) |
| – Discontinued operations (US$'000) | - | (5,106) |
| | (17,755) | (17,191) |
| Weighted average number of outstanding ordinary shares in issue | 51,229,174 | 51,216,279 |
| Basic and diluted loss per share (US$) | | |
| – Continuing operations | (0.3466) | (0.2360) |
| – Discontinued operations | - | (0.0997) |
| | (0.3466) | (0.3357) |

No diluted loss per share is presented as the exercise of the outstanding employee share options would have anti-dilutive effect.

## 12 DIRECTORS' EMOLUMENTS

| | 2008<br>US$'000 | 2007<br>US$'000 |
|---|---|---|
| Fees | 236 | 309 |
| Basic salaries, housing allowances, other allowances and benefits in kind | 565 | 518 |
| Contributions to pension schemes | 21 | 19 |
| Share-based compensation expenses | 298 | 950 |
| | 1,120 | 1,796 |

## 13 EMPLOYEE BENEFITS EXPENSE (INCLUDING DIRECTORS' EMOLUMENTS)

| | 2008<br>US$'000 | 2007<br>US$'000 |
|---|---|---|
| Wages, salaries and bonuses | 14,672 | 11,121 |
| Pension costs – defined contribution plans | 1,356 | 815 |
| Staff welfare | 2,269 | 1,696 |
| Share-based compensation expenses | 955 | 2,460 |
| | 19,252 | 16,092 |
| Attributable to: | | |
| Continuing operations | 19,252 | 15,231 |
| Discontinued operations | - | 861 |
| | 19,252 | 16,092 |

## 14 PROPERTY, PLANT AND EQUIPMENT

| | Buildings situated in the PRC under medium term leases<br>US$'000 | Leasehold improvements<br>US$'000 | Plant and equipment<br>US$'000 | Furniture and fixtures, other equipment and motor vehicles<br>US$'000 | Construction in progress<br>US$'000 | Total<br>US$'000 |
|---|---|---|---|---|---|---|
| Cost | | | | | | |
| As at 1 January 2008 | 17,922 | 4,978 | 9,997 | 8,106 | 398 | 41,401 |
| Exchange differences | 1,185 | (560) | 670 | 334 | 26 | 1,655 |
| Additions | 28 | 841 | 258 | 1,842 | 428 | 3,397 |
| Disposals | (4) | (82) | (1,334) | (421) | (110) | (1,951) |
| Transfers | 178 | - | 46 | 87 | (311) | - |
| As at 31 December 2008 | 19,309 | 5,177 | 9,637 | 9,948 | 431 | 44,502 |
| Accumulated depreciation and impairment | | | | | | |
| As at 1 January 2008 | 4,112 | 2,817 | 5,021 | 3,769 | - | 15,719 |
| Exchange differences | 278 | (341) | 350 | 43 | - | 330 |
| Charge for the year | 952 | 414 | 1,321 | 1,644 | - | 4,331 |
| Disposals | (1) | (79) | (1,334) | (410) | - | (1,824) |
| As at 31 December 2008 | 5,341 | 2,811 | 5,358 | 5,046 | - | 18,556 |
| Net book value | | | | | | |
| As at 31 December 2008 | 13,968 | 2,366 | 4,279 | 4,902 | 431 | 25,946 |

## 14 PROPERTY, PLANT AND EQUIPMENT (CONTINUED)

| | Buildings situated in the PRC under medium term leases US$'000 | Leasehold improvements US$'000 | Plant and equipment US$'000 | Furniture and fixtures, other equipment and motor vehicles US$'000 | Construction in progress US$'000 | Total US$'000 |
|---|---|---|---|---|---|---|
| Cost | | | | | | |
| As at 1 January 2007 | 14,440 | 4,135 | 9,173 | 5,616 | 544 | 33,908 |
| Exchange differences | 945 | 169 | 542 | 341 | 27 | 2,024 |
| Additions | 2,088 | 411 | 124 | 2,012 | 1,172 | 5,807 |
| Disposals | (2) | (137) | (18) | (50) | (131) | (338) |
| Transfers | 451 | 400 | 176 | 187 | (1,214) | – |
| As at 31 December 2007 | 17,922 | 4,978 | 9,997 | 8,106 | 398 | 41,401 |
| Accumulated depreciation and impairment | | | | | | |
| As at 1 January 2007 | 3,199 | 1,918 | 3,415 | 2,502 | – | 11,034 |
| Exchange differences | 214 | 79 | 230 | 151 | – | 674 |
| Charge for the year | 699 | 865 | 822 | 1,091 | – | 3,477 |
| Disposals | – | (45) | (2) | (22) | – | (69) |
| Impairment | – | – | 556 | 47 | – | 603 |
| As at 31 December 2007 | 4,112 | 2,817 | 5,021 | 3,769 | – | 15,719 |
| Net book value | | | | | | |
| As at 31 December 2007 | 13,810 | 2,161 | 4,976 | 4,337 | 398 | 25,682 |

# Notes To The Accounts

## 15 LEASEHOLD LAND

The Group and its jointly controlled entities' interests in leasehold land represent prepaid operating lease payments and are located in the PRC.

| | 2008 US$'000 | 2007 US$'000 |
|---|---|---|
| Cost | | |
| As at 1 January | 6,265 | 4,534 |
| Exchange differences | 413 | 316 |
| Additions | - | 1,415 |
| As at 31 December | 6,678 | 6,265 |
| Accumulated amortisation | | |
| As at 1 January | 437 | 304 |
| Exchange differences | 29 | 22 |
| Amortisation charge (Note 7) | 130 | 111 |
| As at 31 December | 596 | 437 |
| Net book value | | |
| As at 31 December | 6,082 | 5,828 |

## 16 GOODWILL

| | 2008 US$'000 | 2007 US$'000 |
|---|---|---|
| Cost | | |
| As at 1 January | 6,616 | 6,241 |
| Exchange differences | 436 | 375 |
| As at 31 December | 7,052 | 6,616 |

Goodwill is allocated to the Group's jointly controlled entities, SHPL and HBYS, to the extent of US$2,897,000 (2007: US$2,718,000) and US$4,155,000 (2007: US$3,898,000) respectively.

The Group's pharmaceutical business commenced commercial operations in 2001 and in accordance with initial business plans, start-up losses have been expected as the businesses develop. For the purposes of impairment reviews, the recoverable amount of goodwill is determined based on value-in-use calculations. The value-in-use calculations use cash flow projections based on financial budgets approved by management covering a five-year period. Projections in excess of five years are used to take into account increasing market share and growth momentum.

There are a number of assumptions and estimates involved for the preparation of cash flow projections for the period covered by the approved budget. Key assumptions include the expected growth in revenues and gross margin, and pre-tax discount rate of 10% (2007: 10%), to reflect the risks involved. Management prepared the financial budgets taking into account actual and prior year performance and market development expectations. Cash flows beyond that five-year period have been extrapolated using a steady growth rate of 4%. Judgement is required to determine key assumptions adopted in the cash flow projections and changes to key assumptions can significantly affect these cash flow projections.

## 17 TRADEMARKS AND PATENTS

| | 2008<br>US$'000 | 2007<br>US$'000 |
|---|---|---|
| Cost | | |
| As at 1 January | **1,770** | 10,643 |
| Exchange differences | **109** | 624 |
| Additions | **1** | 15 |
| Write-off with respect to discontinued operations | **-** | (9,512) |
| As at 31 December | **1,880** | 1,770 |
| Accumulated amortisation and impairment | | |
| As at 1 January | **1,168** | 9,868 |
| Exchange differences | **46** | 600 |
| Amortisation charge (Note 7) | **191** | 212 |
| Write-off with respect to discontinued operations | **-** | (9,512) |
| As at 31 December | **1,405** | 1,168 |
| Net book value | | |
| As at 31 December | **475** | 602 |

## 18 AVAILABLE-FOR-SALE FINANCIAL ASSET

| | 2008<br>US$'000 | 2007<br>US$'000 |
|---|---|---|
| Unlisted investment, at cost | | |
| As at 1 January | **136** | 128 |
| Exchange differences | **9** | 8 |
| As at 31 December | **145** | 136 |

Available-for-sale financial asset represents a 5% interest in an unlisted company established in the PRC acquired by a jointly controlled entity of the Group.

## 19 DEFERRED INCOME TAX

| | 2008 US$'000 | 2007 US$'000 |
|---|---|---|
| Deferred tax assets | 333 | 256 |
| Deferred tax liabilities | (289) | – |
| Net deferred tax assets | 44 | 256 |

The movements in net deferred income tax assets are as follows:

| | 2008 US$'000 | 2007 US$'000 |
|---|---|---|
| At 1 January | 256 | – |
| Credited/(charged) to the consolidated profit and loss account | | |
| – depreciation allowances | 77 | 256 |
| – withholding tax on unremitted earnings | (289) | – |
| At 31 December | 44 | 256 |

The deferred tax assets and liabilities are offset when there is a legally enforceable right to set off and when the deferred income taxes related to the same fiscal authority.

The potential deferred tax assets in respect of tax losses which have not been recognised in these consolidated accounts amounted to approximately US$13,153,000 as at 31 December 2008 (2007: US$10,984,000).

These unrecognised tax losses can be carried forward against future taxable income and will expire in the following years:

| | As at 31 December | |
|---|---|---|
| | 2008 US$'000 | 2007 US$'000 |
| No expiry date | 27,553 | 17,171 |
| 2008 | - | 6,228 |
| 2009 | 3,737 | 3,737 |
| 2010 | 5,747 | 5,747 |
| 2011 | 6,059 | 6,059 |
| 2012 | 9,624 | 9,624 |
| 2013 | 10,590 | – |
| | 63,310 | 48,566 |

## 20 INVENTORIES

| | 2008<br>US$'000 | 2007<br>US$'000 |
|---|---|---|
| Raw materials | 5,055 | 4,383 |
| Work in progress | 3,698 | 2,501 |
| Finished goods | 5,961 | 4,838 |
| | 14,714 | 11,722 |

## 21 TRADE AND BILLS RECEIVABLES

| | 2008<br>US$'000 | 2007<br>US$'000 |
|---|---|---|
| Trade receivables from third parties | 8,225 | 5,635 |
| Trade receivables from a related party (Note 30(b)) | 145 | 1,900 |
| Bills receivable | 14,062 | 13,637 |
| | 22,432 | 21,172 |

Substantially all the trade and bills receivables are denominated in RMB and are due within one year from the balance sheet date.

The carrying value of trade and bills receivables approximates their fair values due to their short term maturities.

There is no concentration of credit risk with respect to trade and bills receivables as the Group has a large number of customers.

Bills receivable represents non-interest bearing bank acceptance bills with a maturity period of 3 to 6 months.

Movements on the provision for trade receivables are as follows:

| | 2008<br>US$'000 | 2007<br>US$'000 |
|---|---|---|
| At 1 January | 2,005 | 495 |
| Provision for trade receivables | 11 | 1,497 |
| Receivables written off during the year as uncollectible | (39) | (16) |
| Exchange difference | 132 | 29 |
| At 31 December | 2,109 | 2,005 |

## 21 TRADE AND BILLS RECEIVABLES (CONTINUED)

As at 31 December 2008, trade receivables of approximatley US$1,758,000 (2007: US$639,000) were past due but not impaired. These related to a number of independent customers for whom there is no recent history of default. The ageing analysis of these receivables is as follows:

| | 2008 US$'000 | 2007 US$'000 |
|---|---|---|
| Up to 3 months | 750 | 473 |
| 4 to 6 months | 22 | - |
| Over 6 months | 986 | 166 |
| | 1,758 | 639 |

The credit quality of trade receivables neither past due nor impaired has been assessed by reference to historical information about the counterparty default rates. The existing counterparties do not have significant defaults in the past.

## 22 CASH AND BANK BALANCES

| | 2008 US$'000 | 2007 US$'000 |
|---|---|---|
| Cash at bank and in hand | 11,857 | 4,481 |
| Short-term bank deposits (note (a)) | 26,349 | 48,864 |
| | 38,206 | 53,345 |

| | 2008 US$'000 | 2007 US$'000 |
|---|---|---|
| Denominated in: | | |
| US$ | 27,913 | 48,774 |
| RMB (note (b)) | 9,232 | 3,423 |
| UK Pound Sterling | 201 | 468 |
| HK$ | 546 | 531 |
| Euro | 314 | 149 |
| | 38,206 | 53,345 |

(a) The weighted average effective interest rate on short-term bank deposits, with maturity ranging from one week to two months, was 3% (2007: 2%) per annum during the year. Cash at bank earns interest at floating rates based on daily bank deposit rates.

(b) Cash and bank balances denominated in RMB were deposited with banks in the PRC. The conversion of these RMB denominated balances into foreign currencies is subject to the rules and regulations of foreign exchange control promulgated by the PRC government.

## 23 SHARE CAPITAL

### (a) Authorised and issued capital

| | Number of shares of US$1 each | Nominal amount US$'000 |
|---|---|---|
| Authorised: | | |
| As at 1 January 2007, 31 December 2007, 1 January 2008 and 31 December 2008 | 75,000,000 | 75,000 |

| | Number of shares | US$'000 |
|---|---|---|
| Issued and fully paid: | | |
| As at 1 January 2007 | 51,212,121 | 51,212 |
| Issue of shares under share option scheme (note) | 17,053 | 17 |
| As at 31 December 2007, 1 January 2008 and 31 December 2008 | 51,229,174 | 51,229 |

Note:

On 4 October 2007, 17,053 ordinary shares of US$1 each were allotted and issued by the Company at £1.09 each (equivalent to US$2.17 each) for an aggregate cash consideration of approximately US$38,000 upon the exercise of the relevant share options to subscribe for these shares. These new shares rank pari passu in all respects with the then existing shares.

### (b) Share option scheme

#### *(i) Share option scheme of the Company*

On 4 June 2005, the Company adopted a share option scheme (the "HCML Share Option Scheme"), which was subsequently amended by the Board of Directors of the Company on 21 March 2007. Pursuant to the HCML Share Option Scheme, the Board of Directors of the Company may, at its discretion, offer any employees and directors (including executive and non-executive directors but excluding independent non-executive directors) of the Company, holding companies of the Company and any of their subsidiaries or affiliates, and subsidiaries or affiliates of the Company options to subscribe for shares of the Company. As of 31 December 2008, options representing approximately 4.03% of the issued share capital of the Company were granted to a director of the Company and certain employees of the Group and its jointly controlled entities under the HCML Share Option Scheme which are exercisable within a period of ten years from the offer date subject to the vesting schedules of the respective share options.

## 23 SHARE CAPITAL (Continued)

### (b) Share option scheme (Continued)

#### *(i) Share option scheme of the Company (Continued)*

The following share options were outstanding under the HCML Share Option Scheme as at 31 December 2008:

| Name or category of participant | Effective date of grant | Exercise period of share options | Exercise price | Number of shares subject to the options |
|---|---|---|---|---|
| Christian Hogg | 19 May 2006 (note (i) & (ii)) | On Admission to 3 June 2015 | £1.090 | 768,182 |
| 6 employees in aggregate | 19 May 2006 (note (i) & (ii)) | On Admission to 3 June 2015 | £1.090 | 603,683 |
| 2 employees in aggregate | 11 September 2006 (note (ii)) | From 11 September 2006 to 18 May 2016 | £1.715 | 80,458 |
| 1 employee | 23 March 2007 (note (iii)) | From 23 March 2007 to 22 March 2017 | £1.750 | 8,535 |
| 8 employees in aggregate | 18 May 2007 (note (iii)) | From 18 May 2007 to 17 May 2017 | £1.535 | 90,298 |
| 1 employee | 24 August 2007 (note (iii)) | From 24 August 2007 to 23 August 2017 | £1.685 | 256,060 |
| 1 employee | 25 August 2008 (note (iv)) | From 25 August 2008 to 24 August 2018 | £1.260 | 256,146 |
| | | | | 2,063,362 |

## 23 SHARE CAPITAL (Continued)

### (b) Share option scheme (Continued)

#### *(i) Share option scheme of the Company (Continued)*

Movements in the number of share options outstanding and their related weighted average exercise prices are as follows:

| | 2008 | | 2007 | |
|---|---|---|---|---|
| | Average exercise price in £ per share | Number of options | Average exercise price in £ per share | Number of options |
| As at 1 January | 1.26 | 2,418,957 | 1.14 | 2,132,728 |
| Granted | 1.26 | 256,146 | 1.64 | 790,390 |
| Exercised | - | - | 1.09 | (17,053) |
| Lapsed/replaced | 1.38 | (611,741) | 1.32 | (487,108) |
| As at 31 December | 1.23 | 2,063,362 | 1.26 | 2,418,957 |

There is no consideration in connection with all options granted. The Company has no legal or constructive obligation to repurchase or settle the share options in cash. Save as mentioned above, no other share options under the HCML Share Option Scheme were cancelled or exercised or lapsed during the year ended 31 December 2008.

Notes:

(i) The share options were granted on 4 June 2005, conditionally upon the Company's admission which took place on 19 May 2006.

(ii) The share options granted to certain founders of the Company are subject to, amongst other relevant vesting criteria, the vesting schedule of 50% on 19 May 2007 and 25% on each of 19 May 2008 and 19 May 2009. The share options granted to non-founders of the Company are subject to, amongst other relevant vesting criteria, the vesting schedule of one-third on each of 19 May 2007, 19 May 2008 and 19 May 2009.

(iii) The share options granted are subject to, amongst other relevant vesting criteria, the vesting schedule of one-third on each of the first, second and third anniversaries of the date of grant of share options.

(iv) The share options granted are subject to, amongst other relevant vesting criteria, the vesting schedule of 25% on each of the first, second, third and fourth anniversaries of the date of grant of share options.

(v) As at 31 December 2008, the fair value of share options in connection with the 2,063,362 share options outstanding as at the same date remain unvested was amounting to £253,000 (equivalent to US$466,000). The amount is to be recognised as expense of the Group over the remaining vesting periods of the relevant share options as mentioned in the notes (i) to (iv) above. The amount recognised as expenses for the year ended 31 December 2008 amounted to US$925,000 (2007: US$2,460,000).

## 23 SHARE CAPITAL (Continued)

### (b) Share option scheme (Continued)

#### *(i) Share option scheme of the Company (Continued)*

The fair value of options granted under the HCML Share Option Scheme determined using the Binomial Model is as follows

| | Effective date of grant of share options | | | | | |
|---|---|---|---|---|---|---|
| | 19 May 2006 | 11 September 2006 | 23 March 2007 | 18 May 2007 | 24 August 2007 | 25 August 2008 |
| Value of each share option | £1.546 | £0.553 | £0.635 | £0.533 | £0.526 | £0.569 |
| Significant inputs into the valuation model: | | | | | | |
| Exercise price | £1.090 | £1.715 | £1.750 | £1.535 | £1.685 | £1.260 |
| Share price at effective grant date | £2.5050 | £1.7325 | £1.7900 | £1.5400 | £1.6850 | £1.2600 |
| Expected volatility (note) | 38.8% | 38.8% | 40.0% | 40.0% | 35.0% | 35.0% |
| Risk-free interest rate | 4.540% | 4.766% | 4.834% | 5.098% | 5.100% | 4.700% |
| Expected life of options | 1.2 to 3.9 years | 3.4 to 5.3 years | 3.9 to 5.8 years | 3.9 to 5.7 years | 3.2 to 5.1 years | 7.1 to 8.0 years |
| Expected dividend yield | 0% | 0% | 0% | 0% | 0% | 0% |

Note:

For share options granted on or before 18 May 2007, the volatility of the underlying stock during the life of the options is estimated based on the historical volatility of the comparable companies for the past one to two years as of the valuation date, that is, the effective grant date, since there is no or only a relatively short period of trading record of the Company's shares at the respective grant dates.

For share options granted after 18 May 2007, the volatility of the underlying stock during the life of the options is estimated with reference to the volatility of the Company two years prior to the issuance of share options.

## 23 SHARE CAPITAL (Continued)

### (b) Share option scheme (Continued)

#### *(ii) Share option scheme of a subsidiary*

On 6 August 2008, Hutchison MediPharma Holdings Limited ("HMHL"), a subsidiary of the Company, adopted a share option scheme (the "HMHL Share Option Scheme") pursuant to which any employee or director of HMHL and any of its subsidiaries and affiliates is eligible to participate in the HMHL Share Option Scheme subject to the discretion of the board of directors of HMHL. An initial grant of 4,542,000 options to acquire existing shares in HMHL (representing approximately 15.14% of HMHL's existing issued share capital) has been made to more than 60 senior and middle level employees of a subsidiary of HMHL, Hutchison MediPharma Limited ("HMPL"), at an exercise price of US$1.28 per share.

It is the Group's intention that the HMHL Share Option Scheme will replace the HCML Share Option Scheme as the sole share-based incentive programme for HMPL employees.

The following share options were outstanding under the HMHL Share Option Scheme as at 31 December 2008:

| Category of participant | Effective date of grant | Exercise period of share options | Exercise price | Number of shares subject to the options |
|---|---|---|---|---|
| 64 employees in aggregate | 6 August 2008 (note (i)) | From 6 August 2008 to 5 August 2014 | US$1.28 | 4,528,000 |

Movements in the number of share options outstanding and their related weighted average exercise prices are as follows:

| | **2008** | | 2007 | |
|---|---|---|---|---|
| | **Average exercise price in US$ per share** | **Number of options** | Average exercise price in US$ per share | Number of options |
| As at 1 January | **N/A** | **-** | N/A | - |
| Granted | **1.28** | **4,542,000** | N/A | - |
| Lapsed | **1.28** | **(14,000)** | N/A | - |
| As at 31 December | **1.28** | **4,528,000** | N/A | - |

There is no consideration in connection with all options granted. The Group has no legal or constructive obligation to repurchase or settle the share options in cash. Save as mentioned above, no other share options under the HMHL Share Option Scheme were cancelled or exercised or lapsed during the year ended 31 December 2008.

## 23 SHARE CAPITAL (Continued)

### (b) Share option scheme (Continued)

#### *(ii) Share option scheme of a subsidiary (Continued)*

Notes:

(i) The share options granted are subject to, amongst other relevant vesting criteria, the vesting schedule of 25% on each of the first, second, third and fourth anniversaries of the date of grant of share options.

(ii) As at 31 December 2008, the fair value of share options in connection with the 4,528,000 share options outstanding as at the same date remain unvested was amounting to US$122,000. The amount is to be recognised as expense of the Group over the remaining vesting periods of the relevant share options as mentioned in the note (i) above. The amount recognised as expenses for the year ended 31 December 2008 amounted to US$30,000.

The fair value of options granted under the HMHL Share Option Scheme determined using the Binomial Model is as follows:

| | **Effective date of grant of share options 6 August 2008** |
|---|---|
| Value of each share option | US$0.034 |
| Significant inputs into the valuation model: | |
| Exercise price | US$1.280 |
| Share price at effective grant date | US$0.270 |
| Expected volatility (note) | 53% |
| Risk-free interest rate | 3.293% |
| Expected life of options | 4.6 to 5.8 years |
| Expected dividend yield | 0% |

Note:

The volatility of the underlying stock during the life of the options is estimated based on the historical volatility of the comparable companies for the past one to seven years as of the valuation date, that is, the effective grant date.

## 24 TRADE PAYABLES

| | 2008 US$'000 | 2007 US$'000 |
|---|---|---|
| Trade payables due to third parties | **4,984** | 5,016 |
| Trade payables due to a related party (Note 30(b)) | **306** | 287 |
| | **5,290** | 5,303 |

Substantially all the trade payables are denominated in RMB and due within one year from the balance sheet date.

The carrying value of trade payables approximates their fair values due to their short term maturities.

## 25 OTHER PAYABLES AND ACCRUALS

| | 2008 US$'000 | 2007 US$'000 |
|---|---|---|
| Accrued operating expenses | **4,481** | 6,838 |
| Accrued salaries | **2,650** | 1,872 |
| Payments in advance from customers | **1,943** | 1,837 |
| Deferred government incentives | **2,298** | 1,873 |
| Other payables | **7,464** | 4,622 |
| | **18,836** | 17,042 |

## 26 SHORT-TERM BANK LOANS

| | 2008 US$'000 | 2007 US$'000 |
|---|---|---|
| Short-term bank loans – interest bearing | **7,606** | 6,564 |
| Weighted average effective interest rate | **6.58%** | 6.09% |

The short-term bank loans are unsecured and denominated in RMB. The carrying amount of the short-term bank loans approximates their fair values.

## 27 NOTE TO THE CONSOLIDATED CASH FLOW STATEMENT

Reconciliation of loss for the year to net cash used in operations

| | 2008<br>US$'000 | 2007<br>US$'000 |
|---|---|---|
| Loss for the year | (16,258) | (15,966) |
| Adjustments for: | | |
| Taxation charge | 1,503 | 838 |
| Share-based compensation expenses | 955 | 2,460 |
| Amortisation of trademarks and patents | 191 | 212 |
| Amortisation of leasehold land | 130 | 111 |
| Impairment on property, plant and equipment | - | 603 |
| Write-off of inventories | 225 | 359 |
| Provision for inventories | 6 | 326 |
| Provision for trade and other receivables | 11 | 1,734 |
| Depreciation on property, plant and equipment | 4,331 | 3,477 |
| Loss on disposal of property, plant and equipment | 110 | 269 |
| Interest income | (1,221) | (937) |
| Interest expense | 528 | 367 |
| Operating loss before working capital changes | (9,489) | (6,147) |
| Changes in working capital: | | |
| – increase in inventories | (3,156) | (2,419) |
| – decrease/(increase) in trade and bills receivables | 115 | (5,129) |
| – increase in other receivables and prepayments | (540) | (244) |
| – (decrease)/increase in trade payables | (325) | 1,837 |
| – increase in other payables and accruals | 962 | 4,414 |
| Net cash used in operations | (12,433) | (7,688) |
| Attributable to: | | |
| Continuing operations | (12,433) | (5,494) |
| Discontinued operations | - | (2,194) |
| | (12,433) | (7,688) |

## 28 COMMITMENTS

### (a) Capital commitments

The Group had the following capital commitments not provided for at the balance sheet date:

| | 2008<br>US$'000 | 2007<br>US$'000 |
|---|---|---|
| Property, plant and equipment | | |
| Authorised but not contracted for | - | - |
| Contracted but not provided for | 164 | 252 |
| | 164 | 252 |

## 28 COMMITMENTS (Continued)

### (b) Operating lease commitments

The Group leases various factories, offices and retail stores under non-cancellable operating lease agreements.

As at 31 December 2008, the future aggregate minimum lease payments in respect of land and buildings under non-cancellable operating leases were as follows:

| | 2008<br>US$'000 | 2007<br>US$'000 |
|---|---|---|
| Not later than one year | 801 | 1,097 |
| Later than one year and not later than five years | 2,472 | 2,621 |
| Later than five years | 3,317 | 4,093 |
| | 6,590 | 7,811 |

## 29 JOINTLY CONTROLLED ENTITIES

The Group has interests in two jointly controlled entities. Particulars of the jointly controlled entities of the Group are set out in Note 33. The following amounts represent the Group's share of the assets, liabilities, income, results, and commitments of the jointly controlled entities. They are included in the consolidated balance sheet and consolidated profit and loss account:

| | 2008<br>US$'000 | 2007<br>US$'000 |
|---|---|---|
| Assets | | |
| Non-current assets | 28,116 | 27,934 |
| Current assets | 43,204 | 33,332 |
| | 71,320 | 61,266 |
| Liabilities | | |
| Non-current liabilities | 13,942 | 13,178 |
| Current liabilities | 20,023 | 24,726 |
| | 33,965 | 37,904 |
| Net assets | 37,355 | 23,362 |
| Income | 75,144 | 57,648 |
| Expenses | (67,828) | (52,173) |
| Profit after taxation | 7,316 | 5,475 |
| Capital commitments | - | 138 |
| Operating lease commitments | 63 | 151 |

There are no contingent liabilities relating to the Group's interests in the jointly controlled entities and these jointly controlled entities did not have any material contingent liabilities as at 31 December 2008.

# Notes To The Accounts

## 30 SIGNIFICANT RELATED PARTY TRANSACTIONS

Save as disclosed above, the Group has the following significant transactions during the year with related parties which were carried out in the normal course of business at terms determined and agreed by the relevant parties:

| | 2008 US$'000 | 2007 US$'000 |
|---|---|---|
| (a) Transactions with related parties: | | |
| Continuing operations: | | |
| Revenue: | | |
| Sales of goods | | |
| – Fellow subsidiaries | - | 5,393 |
| Expenses: | | |
| Purchase of goods and raw materials | | |
| – A minority shareholder of a subsidiary | - | 289 |
| Sub-contracting charges | | |
| – A minority shareholder of a subsidiary | - | 624 |
| Management service fee | | |
| – An intermediate holding company | 876 | 873 |
| Technology fee | | |
| – A minority shareholder of a subsidiary | 31 | 138 |

No transactions have been entered into with the directors of the Company (being the key management personnel) during the years ended 31 December 2007 and 2008 other than the emoluments paid to them (being the key management personnel compensation) as disclosed in Note 12.

## 30 SIGNIFICANT RELATED PARTY TRANSACTIONS (CONTINUED)

| | 2008<br>US$'000 | 2007<br>US$'000 |
|---|---|---|
| (b) Balances with related parties included in: | | |
| Trade receivable from a related party (Note 21): | | |
| – A fellow subsidiary | 145 | 1,900 |
| Trade payables due to a related party (Note 24): | | |
| – A minority shareholder of a subsidiary | 306 | 287 |
| Amounts due to related parties: | | |
| – Immediate holding company | 773 | 269 |
| – Minority shareholders of a subsidiary | 201 | 227 |
| | 974 | 496 |

Balances with related parties are unsecured, interest-free and repayable on demand. The carrying value of balances with related parties approximates their fair values due to their short term maturities.

(c) Others:

During the year, the Group entered into an agreement with a fellow subsidiary of the Group and a third party common distributor of the Group (the "Distributor") whereby it was agreed that an amount due from the fellow subsidiary to the Group of approximately US$800,000 be assigned to the Distributor in order to facilitate central collection of the relevant trade receivables from the Distributor.

## 31 ULTIMATE HOLDING COMPANY

The Company's directors regard Hutchison Whampoa Limited, a company incorporated and listed in Hong Kong, as being the ultimate holding company of the Company.

## 32 APPROVAL OF ACCOUNTS

The consolidated accounts set out on pages 44 to 88 were approved by the Board of Directors on 13 March 2009.

# Notes To The Accounts

## 33 PARTICULARS OF PRINCIPAL SUBSIDIARIES AND JOINTLY CONTROLLED ENTITIES AS AT 31 DECEMBER 2008

| Name | Place of establishment and operation | Nominal value of issued ordinary share capital/ registered capital | Equity interest attributable to the Group | | Type of legal entity | Principal activities |
|---|---|---|---|---|---|---|
| | | | As at 31 December | | | |
| | | | **2008** | 2007 | | |
| **Subsidiaries** | | | | | | |
| Hutchison Healthcare Limited | The PRC | RMB166,250,000 | **67.97%** | 67.97% | Limited liability company | Manufacture and distribution of healthcare products |
| Hutchison MediPharma Limited | The PRC | US$20,500,000 | **100%** | 100% | Limited liability company | Research and development of pharmaceutical products |
| Sen Medicine Company Limited | UK | £1 | **100%** | 100% | Limited liability company | Retail and distribution of TCM based consumer products |
| Sen Medicine Company (France) S.A.R.L. | France | Euro7,500 | **100%** | – | Limited liability company | Distribution of TCM based consumer products |
| **Jointly controlled entities** | | | | | | |
| Shanghai Hutchison Pharmaceuticals Limited | The PRC | RMB88,000,000 | **50%** | 50% | Limited liability company | Manufacture and distribution of TCM products |
| Hutchison Whampoa Guangzhou Baiyunshan Chinese Medicine Company Limited | The PRC | RMB200,000,000 | **37.5%** | 37.5% | Limited liability company | Manufacture and distribution of TCM products |

# Information For Shareholders

## Listing
The Company's ordinary shares are listed on the Alternative Investment Market operated by London Stock Exchange plc

## Code
HCM

## Financial Calender

| | |
|---|---|
| Closure of Register of Members | 7 May 2009 to 8 May 2009 |
| Annual General Meeting | 8 May 2009 |
| Interim Results Announcement | July 2009 |

## Registered Office
P.O. Box 309, Ugland House
Grand Cayman, KY1-1104
Cayman Islands
Telephone: +1 345 949 8066
Facsimile: +1 345 949 8080

## Principal Executive Office
21st Floor, Hutchison House
10 Harcourt Road
Hong Kong
Telephone: +852 2121 8200
Facsimile: +852 2121 8281

## Share Registrar
Computershare Investor Services (Channel Islands) Limited
P.O. Box 83, Ordnance House
31 Pier Road, St. Helier
Jersey, Channel Islands JE4 8PW
Telephone: +44 (0)1534 825200
Facsimile: +44 (0)1534 825250

## Depositary
Computershare Investor Services PLC
The Pavilions
Bridgwater Road
Bristol BS13 8AE
United Kingdom
Telephone: +44 (0)870 703 6348
Facsimile: +44 (0)870 703 6114

## Correspondence Address
22nd Floor, Hutchison House
10 Harcourt Road
Hong Kong
Telephone: +852 2128 1188
Facsimile: +852 2128 1778

## Shareholders Contact
Please direct enquires to:

- Correspondence address:
  22nd Floor, Hutchison House
  10 Harcourt Road
  Hong Kong
  Attn: Ms Edith Shih
  Non-executive Director
  & Company Secretary
- Facsimile: +852 2128 1778
- E-mail: ediths@hwl.com.hk
- Registered office

## Investor Information
Corporate press releases, financial reports and other investor information on the Company are available online at the Company's website.

## Investor Relations Contact
Please direct enquires to:
E-mail: ir@chi-med.com
Telephone: +852 2121 8200
Facsimile: +852 2121 8281

## Website Address
www.chi-med.com

## Forward Looking Statements
This annual report contains forward looking statements. Forward looking statements include statements concerning plans, objective goals and strategies, future events or performance, and underlying assumptions and other statements that are other than statements of historical fact. These statements are subject to uncertainties and risks including but not limited to, the ability to meet on-going capital needs, products and service demand and acceptance, changes in technology, economic conditions, the impact of competition, the need to protect proprietary rights to technology, government regulation and other risks as noted herein and in statements filed from time to time with applicable securities regulating authorities.