RISK FACTORS

If any of the possible events described below occurs, the business operation, financial condition or results of operation of the Group could be materially and adversely affected and the market price of the Shares could fall significantly.

We are principally engaged in pharmaceutical distribution businesses in the PRC. Please refer to the section headed "Business – Our business model" for details. In this relation, we believe that there are certain risks involved in our operations. Many of these risks are beyond our control and can be categorised into: (i) risks relating to the business; (ii) risks relating to the industry; and (iii) risks relating to the PRC. Particularly in light of our business model, the most significant risk factors we face are highlighted as below, which may impair our business operation and profitability, and our business and growth may thereby not be sustainable:

- we rely on our suppliers to provide us the pharmaceutical products with market potential for distribution to Distributor Customers, and also rely on our major Distributor Customers to sell the products, whose ultimate customers mainly comprise hospitals and medical institutions in the PRC in accordance with the geographical exclusivity of our products, where we however do not have any long-term agreement or commitment with such suppliers and Distributor Customers;

- a majority of our products are subject to the up-coming collective tendering process and our supplies may fail to win the collective tendering process for securing orders from public hospitals and medical institutions, which may result in a significant impact on our future profit;

- the pharmaceutical industry in the PRC is highly regulated, for example, a substantial amount of the products distributed by us are subject to government price controls or other price restrictions in the PRC;

- certain of the major products we distributed during the Track Record Period and as at the Latest Practicable Date were antibiotics, and our business and results of operation may be adversely affected by any government control over the use of antibiotics and hence the resultant decrease in demand for such products;

- a substantial amount of deposits and prepayments were made to suppliers for securing the exclusive distribution rights of those products with market potential, and we may not be able to recover any or all of the deposit amount paid to suppliers if we act in breach of our obligations provided in the distribution agreements, or if our suppliers' financial condition deteriorates or there is any dispute between our suppliers and us;

- being merely a pharmaceutical distributor, the quality of the products distributed by us is beyond our control and we may face legal or administrative proceedings as a result of any alleged inferior quality of the products we distribute; and

- we may face the claim from any of our suppliers or Distributor Customers for any liability and hence any resultant negative publicity on our Group if we fail to perform the obligations under the distribution agreement.

RISKS RELATING TO THE BUSINESS

We do not enter into any long-term agreement with our suppliers, and may be materially and adversely affected if we fail to maintain or establish business relationships with suppliers (particularly where we rely on our key suppliers) in the pharmaceutical distribution operations

We typically distribute products pursuant to distribution agreements entered into between our Group and our suppliers. However, we do not enter into any long-term contractual agreement with our suppliers, where the term of the agreements with our suppliers generally ranges from one year to three years. Accordingly, we cannot assure you that the existing suppliers will continue to sell products to us on commercially reasonable terms, or at all. We also cannot assure you that we will be able to maintain or extend relationships with existing suppliers when the agreements with them expire. Our distribution agreements with suppliers may be terminated from time to time due to various reasons beyond our control.

During the Track Record Period, our purchases from our top five suppliers amounted to approximately HK$111.7 million, HK$125.9 million and HK$60.3 million, respectively, which represented approximately 85.9%, 91.8% and 92.9% of our total purchases during the corresponding periods. In particular, purchases from our single largest supplier for each of the two years ended 31 December 2011 and 2012 and the second largest supplier for the six months ended 30 June 2013, namely, Baoding Huida Pharmaceutical Company Limited (保定滙達醫藥有限公司) (whose business relationship with our Group has been replaced by Baoding Zhongcheng Huida Pharmaceutical Trading Company Limited (保定中誠匯達醫藥貿易有限公司) since March 2012), accounted for approximately 39.9%, 50.5% and 33.7%, respectively, of our total purchases for each of the two years ended 31 December 2011 and 2012 and for the six months ended 30 June 2013. If we fail to maintain or extend our relationships with the existing suppliers (particularly where our business is dependent on the purchase of pharmaceutical products from our key suppliers) and may not be able to establish relationships with new suppliers, our revenue and profitability could significantly decrease, and our financial condition and results of operations could be materially and adversely affected.

We are in lack of long-term agreements with or commitments from the Distributor Customers, any disruption or termination of business relationships with our major Distributor Customers especially Type 1 Distributor Customers may have a material adverse on our business and operating results

We generally sell the pharmaceutical products to the Distributor Customers which then distribute or on-sell those products to sub-distributors and/or ultimate customers which mainly comprise hospitals and medical institutions in the PRC in accordance with the geographical exclusivity of our products. For each of the two years ended 31 December 2011 and 2012 and for the six months ended 30 June 2013, our top five Distributor Customers collectively accounted for approximately 58.4%, 69.4% and 70.9%, respectively, of our total revenue. In particular, our Type 1 Distributor Customers generated the largest proportion of our total revenue. The number of Type 1 Distributor Customers increased from 25 to 34 during the Track Record Period. For each of the two years ended 31 December 2011 and 2012 and for the six months ended 30 June 2013, the revenue generated from Type 1 Distributor Customers represented approximately 73.6%, 87.5% and 91.0%, respectively, of our total revenue.

Whereas we do not enter into any distribution agreement with Type 3 Distributor Customers, we normally enter into distribution agreement with our Type 1 Distributor

Customers and Type 2 Distributor Customers for a term ranging from one year to two years. In other words, we merely enter into short-term agreements or commitments with the Distributor Customers, which may fail to protect us from the impact of a reduction in the demand for the products we distribute as a result of various reasons beyond our control. We cannot assure you that these Distributor Customers will renew their agreements with us, or otherwise retain their business relationships with us, and that these Distributor Customers will continue to purchase our products at current volume or prices in the future. In the event that any of these Distributor Customers decide to choose our competitors and terminate their business relationships with us and we fail to expand our business with the existing Distributor Customers or to attract new customers, we may experience no growth or even decrease in our revenue, and hence our business, financial condition and results of operations could be materially and adversely affected. Furthermore, any significant change in the business developments or financial condition of any of these key Distributor Customers may require us to assume more credit risk relating to receivables from that Distributor Customer, or make us restrict or terminate business with that Distributor Customer, which could also result in a material adverse effect on our business operation and financial condition.

Our suppliers may not be always successful in winning the tendering process which may hence affect our product penetration to the public hospitals in the PRC

A majority of our products are distributed through our Distributor Customers to the ultimate customers which are mainly public hospitals and medical institutions in the PRC. According to the relevant PRC laws and regulations, public hospitals and other public healthcare institutions are required to purchase substantially all pharmaceutical products through a collective tendering process, which is operated and organised by the provincial government agencies. Pharmaceutical products that have previously been selected in the collective tendering processes must participate and win in the collective tendering processes in the subsequent tender period before new purchase orders can be issued. Factors considered in assessing tenders include, among other things, the quality and price of the products and the service and reputation of the manufacturers. We normally enter into distribution agreement with our Type 1 Distributor Customers and Type 2 Distributor Customers for a term ranging from one year to two years, which may depend on the tender period of the relevant pharmaceutical product(s). In addition, assisting our suppliers to win the collective tendering process is one of the crucial elements to our business. During the Track Record Period, the revenue generated from our products that have won the collective tendering process represented approximately 97.7%, 98.2% and 96.8% of our total revenue for the corresponding periods and those products are subject to the upcoming collective tendering. If our suppliers were unsuccessful in these collective tendering processes, our sales to public hospitals through the Distributor Customers would inevitably decrease, which could result in a material adverse effect on our business, financial condition and results of operations.

Our products are subject to price controls and we do not have full discretion over the pricing of such products, where such price controls or other price restrictions may affect our revenue and gross profit margin of the affected products

Downward adjustment to the maximum product price may adversely affect our revenue

Pharmaceutical products that are included in the Medical Insurance Drugs Catalogs are subject to government price control in the form of fixed retail prices or maximum retail prices and periodic downward adjustments in the pricing. As at the Latest Practicable Date, 42 out of our 55 products were included in the Medical Insurance Drugs Catalogs, and were therefore

subject to price control in the PRC. Sales of products included in the Medical Insurance Drugs Catalogs, which comprise one of our major products, Levocarnitine Injection (左卡尼汀注射液), accounted for approximately 85.0%, 93.7% and 93.0% of our total revenue for each of the two years ended 31 December 2011 and 2012 and for the six months ended 30 June 2013, respectively. Please refer to the section headed "Business – Price controls" showing the impact on our major products as a result of the imposition of the retail price ceiling by NDRC or Zhejiang Provincial Price Bureau with effect from 25 February 2011, 28 March 2011, 21 March 2012, 8 October 2012 and 6 February 2013, respectively.

Further, pursuant to the Circular on Strengthening the Reform of Pricing for Medicines and Medical Services in County Level Public Hospitals (關於推進縣級公立醫院醫藥價格改革工作的通知) jointly issued by NDRC, the Ministry of Health and the Ministry of Human Resources and Social Security on 3 September 2012, the prices of medicines sold by the selected pilot hospitals shall be reduced by approximately 15% after the reform. In the event that there is a hypothetical downward adjustment to the pricing of the products we distribute by 15% and we fail to renegotiate with the relevant suppliers to lower the purchase prices and/or renegotiate with the relevant Distributor Customers to reset the selling prices to mitigate the impact of price adjustments on our products, our revenue may be reduced by 15% accordingly, which may, in turn, result in a gross loss of our Group. Therefore, any control over and adjustment to the maximum retail price of a pharmaceutical product by the PRC government authorities, if significant, could have a corresponding impact on the wholesale price of that pharmaceutical product and our revenue as a whole. The PRC government may further lower the retail price ceilings of pharmaceutical products from time to time to make healthcare more affordable to the public. Such trend of price adjustments may continue in the future as a result of the PRC government's imposition of any further regulatory control measure on the price of the products our Group distribute, which may adversely affect the retail price of such products and hence our profitability.

Demand for the products we distribute may decline if such products are no longer under price control or the scope of reimbursement is to be limited

Patients in the PRC purchasing pharmaceutical products that are listed in the Medical Insurance Drugs Catalogs are eligible for full or partial reimbursement under national and provincial medical insurance, work injury insurance and maternity insurance programs. However, the PRC state and provincial authorities may review the National Medical Insurance Drugs Catalog and the Provincial Medical Insurance Drugs Catalogs periodically and may remove a listed product based on various factors, including treatment requirements, frequency of use, efficacy and price. In addition, some of our products listed on the Medical Insurance Drugs Catalogs are subject to limitation on the scope of reimbursement such as the type of diseases or insurance that the patients may claim for. Subject to adjustment by the relevant state and provincial regulators, if the scope of reimbursement is further limited by the types of diseases or insurance that the patients may claim for, it may affect the demand for our products that are subject to such limitation and subsequently affect the sales volume and retail prices of such products.

Certain of the major products we distributed during the Track Record Period and as at the [Latest Practicable Date] were antibiotics, and our business and results of operation may be adversely affected by any government control over the use of antibiotics

NHFPC issued the Campaign Schemes to Regulate the Use of Antibiotics for the Years of 2011, 2012 and 2013 (2011年全國抗菌藥物臨床應用專項整治活動方案, 2012年全國抗菌藥物臨床應用專項整治活動方案 and 2013年全國抗菌藥物臨床應用專項整治活動方案), respectively, on 18 April 2011, 5 March 2012 and 6 May 2013, and the Administrative

Measures on the Clinical Use of Antibiotics (抗菌藥物臨床應用管理辦法) on 24 April 2012, which, among other things, (i) classify antibiotics into three categories, including non-limited use, limited use and special use, (ii) limit the number of antibiotics used by hospitals on different levels; and (iii) require the provincial health authorities to formulate their catalogues of the antibiotics on their own. According to the Administrative Catalogue of the Clinical Use of Antibiotics of Zhejiang Province (2012 version) (浙江省抗菌藥物臨床應用分級管理目錄(2012版)) issued by Zhejiang Provincial Health Bureau on 19 July 2012, certain of the major products distributed by us during the Track Record Period and as at the [Latest Practicable Date], including Cefoxitin Sodium for Injection (注射用頭孢西丁鈉), Cefodizime Sodium for Injection (注射用頭孢地嗪鈉), Isepamicin Sulfate Injection (硫酸異帕米星注射液), Cefixime Dispersible Tablet (頭孢克肟分散片) and Ceftizoxime Sodium for Injection (注射用頭孢唑肟鈉), fell within the category of limited use. In particular, such restriction on the usage of antibiotics led to a decline in demand of Isepamicin Sulfate Injection (硫酸異帕米星注射液) from hospitals and hence a decrease in its sales amount, which had inevitably affected our results of operation for the year ended 31 December 2012. Our business and results of operation may be adversely affected if we are going to acquire any new exclusive distribution right of pharmaceutical products in relation to antibiotics in the future which may however be caught by those laws rule or regulations governing the use of antibiotics and even fall into the category of limited use.

If we fail to recover the deposits paid to our suppliers, our operation results and financial conditions may be adversely and materially affected

We may not be able to recover any or all of the deposit amount paid to our suppliers in case of our inability to meet the prescribed sales targets and/or of any cannibalisation by us whatsoever in contravention of the terms and conditions of the distribution agreements

Type 1 Suppliers and Type 2 Suppliers require us to pay a certain amount of, among other things, deposits as a condition of acquiring the distribution rights of specific products to ensure our commitment to meet the prescribed sales target. Otherwise, suppliers are entitled to forfeit the deposits we have paid or to terminate the agreement with us, as the case may be. In fact, we may not be able to meet the sales targets as respectively prescribed by the suppliers at all times. During the Track Record Period, we failed to satisfy the prescribed sales targets of four of our suppliers under the distribution agreements respectively entered into between those suppliers and us. Subsequently, our distribution agreement with one of those suppliers was terminated after its expiry on 30 December 2012 without renewal. Please refer to the section headed "Business – Our business model – Phase 2 – Procurement of products from our suppliers – Sales target from our suppliers" for details. Whether or not we are able to achieve the prescribed sales target from time to time provided under the distribution agreements relies on the market condition and this market demand of the product(s) we distribute. There is no assurance that the deposit paid to the suppliers as required under the distribution agreement would be, fully or partially, recovered or that such supplier would not claim us for any liability as result of our failure to achieve the prescribed sales target despite termination of the agreement. On the other hand, if our Group were to cannibalise the market in other provinces or regions than those provided in the distribution agreements, our paid deposits shall be subject to deduction or even forfeiture in the manner as set out in the distribution agreements. Under such circumstances, failure to recover any or all of our paid deposit would inevitably have a material adverse impact on our operation results and financial conditions.

We may not be able to recover the deposits paid to our suppliers if we cease business with such suppliers and their own financial condition deteriorates or there is any dispute between those suppliers and us

Deposits paid to suppliers increased from RMB12,834,000 (equivalent to approximately HK$15,817,000) as at 31 December 2011 to RMB26,488,000 (equivalent to approximately HK$33,456,000) as at 30 June 2013. Normally, the deposits paid to suppliers will be returned in full within the prescribed period after termination of the distribution agreement upon the terms and conditions of the relevant distribution agreement(s). However, whether or not our suppliers would remain financially potent in the future is not certain. Also, we have no assurance that the favourable relationships we have established with our suppliers over the years will persist. In the event that we cease business with our suppliers, where our suppliers' own financial condition deteriorates or there is any dispute between those suppliers and us, for example, on the product quality issue or the satisfaction of any license requirement, they may not be able or willing to refund any or all of the deposits we have previously paid to them. Under such circumstances, our Group's financial condition and operation results would be materially and adversely affected, especially in light of the substantial amount of the deposits paid to our suppliers as described above.

The brand name of the products we distribute as well as our corporate image and reputation may be materially and adversely affected as a result of any legal or administrative proceedings relating to the alleged inferior quality of the products we distribute and also the existence of counterfeit products in the pharmaceutical industry

The quality of the products we distribute is not guaranteed, and any undesirable side effect or harm caused by such products could materially and adversely affect our corporate image

We are only a pharmaceutical distributor and the quality of the products distributed by us, which may be affected during the processes of production, transportation, storage, warehousing and usage, is not under our control. As we are not involved in any pharmaceutical manufacturing process, we do not have any facilities to conduct any laboratory or clinical testing of the quality of the pharmaceutical products due to the constraint of the nature of our business and operation. Despite the fact that we have engaged Hangzhou Institute of Drug Control (杭州市藥品檢驗所) ("**HIDC**"), a government controlled certified testing center in Hangzhou province, the PRC, to conduct clinical testing for our pharmaceutical products, such clinical testing is merely carried out for our newly acquired product with annual sales estimated to be more than 3% of our total revenue, and also our existing major products with the annual sales of more than 3% of our total revenue. Please refer to the section headed "Business – Quality control – Incidents related to quality of the products we distributed" for details. In other words, not each and every product of our Group is to be covered under such clinical testing, and the quality of all the products we distribute cannot be guaranteed accordingly. Under such circumstances, those products not being subject to the HIDC clinical testing may contain such fundamental quality problems as undesirable side effects or harm that are unknown to us. This will not only adversely affect the reputation of the products we distribute, our corporate image as well as our sales volume, but may also lead to claims or potential litigation against us.

We may face legal or administrative proceedings and hence any adverse publicity as a result of the alleged inferior quality of the products we distribute

Our Group faced one claim arising from distribution agreements in March 2010 and one administrative penalty in September 2010 relating to the quality of the pharmaceutical products as supplied by pharmaceutical manufactures for our distribution. Please refer to the

section headed "Business – Quality control – Incidents related to quality of the products we distributed" for details. Adverse publicity which may arise from the legal or administrative proceedings whatsoever relating to the alleged inferior quality of the pharmaceutical products we distribute, regardless of whether it is meritless or unfounded, may damage the image of those products we distribute and hence our reputation, which may in turn cause our Distributor Customers to lose confidence in the brands of those products we distribute and hence our Group, and not to purchase the products concerned. Also, any of such proceedings and their respective consequences could be costly and divert management's attention from our business. Further, even if the responsibility lies with our manufacturers or suppliers of the defective products, there is no assurance that we will be able to fully recover from such manufacturer or supplier the relevant compensation or at all. Our failure to recover such compensation in full or failure of those manufacturers or suppliers to pay us in a timely manner may have a material adverse effect on our business, financial condition, results of operations and prospects.

Existence of counterfeit products in the market may materially and adversely affect our business and prospects

We cannot assure you that there will be no individual or entity which has the capability and determination to manufacture counterfeit pharmaceutical products imitating our suppliers' products. Any unintentional sale of these products by us in our distribution, or the sale of counterfeit pharmaceutical products by others illegally under the brand names of any of our suppliers' products, especially where it results in adverse side effects to consumers, may subject us to negative publicity, fines and other administrative penalties or even result in litigation against us. Moreover, consumers may buy counterfeit pharmaceutical products that are in direct competition with our products sourced from our suppliers, which could have a material adverse effect on our business, financial condition, results of operations and prospects.

We do not have product liability insurance and may not be adequately protected from any product liability claim and/or potential loss

Taking into consideration the fact that (i) we are primarily engaged in distribution of pharmaceutical products in the PRC but not involved in any pharmaceutical manufacturing process; and (ii) so far as we are aware, maintaining product liability insurance for pharmaceutical products and insurance relating to the release of hazardous materials is not a common industry practice in the PRC, we do not maintain product liability insurance or insurance covering potential liability relating to the quality of the pharmaceutical products we distribute. Therefore, any material loss or damage caused by any claim against us for the quality of pharmaceutical products, or sale of counterfeit pharmaceutical products imitating our suppliers' products, which are alleged or proven to be contaminated, defective, harmful, ineffective or unsafe, could cause us to incur substantial costs and also divert our allocation of resources. This may therefore materially and adversely affect our business, financial condition and results of operations.

We may be involved in any claim initiated by our Distributor Customers against any alleged breach of terms of the distribution agreements such as infringement of the exclusive right of product distribution granted to our Distributor Customers, which could divert our management's attention from daily business operation

Pursuant to the distribution agreements between our Distributor Customers and us, our Distributor Customers are required to satisfy a minimum order quantity commitment, failing which we are entitled to forfeit distribution right of the defaulting Distributor Customer and to grant the distribution right to a third party in those markets not yet explored by the defaulting

Distributor Customer. On 25 June 2012, a former Type 2 Distributor Customer (which failed to commit the agreed minimum order quantity requirement under our distribution agreement) instituted legal proceedings against Zhejiang Xin Rui Pharmaceutical at Hangzhou City Jianggan District People's Court (杭州市江干區人民法院) regarding, among other things, the alleged infringement by Zhejiang Xin Rui Pharmaceutical of the exclusive right of a pharmaceutical product granted to that former Type 2 Distributor Customer in contravention of the exclusivity provision under the distribution agreement in question. Please refer to the section headed "Business – Legal proceedings and non-compliance – (i) Legal proceedings relating to our Group" for details. In this connection, given the exclusivity provision contained in the distribution agreement we generally enter into with our Distributor Customers, even if a Distributor Customer fails to satisfy the required minimum order quantity commitment provided under the distribution agreement, we may face claims from time to time initiated by our Distributor Customers for the alleged breach of the terms of the distribution agreements by us. Any of such proceeding (regardless of whether it is meritless or unfounded) and its consequences could be costly and could divert the attention of our management from the daily operation of business. If any of legal proceedings against us is successful, it may inevitably result in a material adverse effect on our business and reputation.

We may not be able to sustain the gross profit margins at the levels recorded during the Track Record Period

Our gross profit margin increased from approximately 14.6% for the year ended 31 December 2011 to approximately 22.1% for the six months ended 30 June 2013. This was mainly attributable to our Group's diversification of the product portfolio during the Track Record Period associated with the increase in gross profit margin of capsule drugs. Please refer to the section headed "Financial information – Description of principal items of results of operations – Gross profit" for details. However, diversification of the product portfolio may result in different gross profit margin recorded for different products, particularly where market potential varies from product to product depending on, for example, the market conditions and the competitive landscape of the product(s) we distribute. Our profitability and results of operation may therefore vary significantly from time to time as a result of any change in the combination of products sold during the relevant period. In this relation, there is no assurance that we will be able to maintain and secure the gross profits margins at the levels recorded during the Track Record Period. In addition, whether or not our gross profit margin is sustainable may be affected by various factors such as changes in consumer demand, government price control policies and prevailing market conditions, which are to a large extent beyond our control. Accordingly, we cannot guarantee that our gross profit margins will not fluctuate from time to time. If there is any decline in our gross profit margins in the future, our profitability and financial condition may be adversely affected.

We experienced net cash outflow from operating activities for the years ended 31 December 2011 and 2012

We had net cash outflow from our operating activities of approximately HK$96,000 and HK$6,972,000, respectively, for each of the two years ended 31 December 2011 and 2012 primarily due to an increase in trade and other receivables as a result of, among other things, the deposits and/or prepayments (as the case may be) made to our suppliers to secure the exclusive distribution rights of products with market potentials for the sake of our business expansion. Please refer to the section headed "Financial information – Liquidity and capital resources – Cash flows – Net cash (used in) from operating activities" for details. We cannot assure that we will not experience periods of net cash outflow from operating activities in the future, particularly where we are required to make such deposit payment to secure the

distribution rights of the existing products and acquire the distribution rights of the new products with the market potential for business expansion (as a result of our suppliers' refusal of the proposed corporate guarantee arrangements in substitution of the deposit payment) and also such prepayment to ensure the stable supply of the products, respectively, for improvement of our profitability in the long run, where we may experience the same after [●]. If we are unable to finance our operations continuously from funds generated from operating activities and bank borrowings, our operations and financial position could be materially and adversely affected.

We are subject to credit risk in respect of trade debtors and bills receivables

During the Track Record Period, the general credit term granted to our Distributor Customers ranged from 30 to 90 days pursuant to the distribution agreements. As at 31 December 2011, 31 December 2012 and 30 June 2013, our trade and bills receivables were approximately HK$48,149,000, HK$41,701,000 and HK$45,506,000, which accounted for approximately 33.1%, 25.1% and 23.8% of our total assets, respectively. There is no assurance that we will be able to collect all trade and bills receivables from all of our Distributor Customers in full or in a timely manner. Should a significant number of our Distributor Customers fail to settle their trade and bills receivables in full for any reason, we may incur impairment losses and our results of operations and financial position could be materially and adversely affected.

We rely on the market in the PRC, especially in the Eastern China regions, for the bulk of our sales. Any adverse change in the economic, political or social conditions in such cities and provinces may materially and adversely affect our business, financial condition and results of operations

The PRC's economy differs from the economies of most developed countries in many aspects, including the amount of government intervention, level of infrastructure development, level of capital reinvestment, control of foreign exchange and allocation of resources. Over the past two decades, the PRC government has undertaken reform measures in its economic and political systems, resulting in a significant economic growth in the PRC. However, there is no assurance that the PRC government will continue to pursue such reforms or that all the reform measures implemented will be effective. During the Track Record Period, all of our operations are conducted in the PRC and we generated all the sales in the PRC, which would remain our target market in the future. In particular, a significant proportion of our revenue was generated from sales in the regions of Eastern China, which tended to have higher urbanisation rates and be more economically developed. During the Track Record Period, a majority of our Group's revenue was generated from Zhejiang province. Our sales made in the Zhejiang province for each of the two years ended 31 December 2011 and 2012 and the six months ended 30 June 2013 accounted for approximately 74.7%, 80.4% and 79.1% of our total turnover for the respective periods. Our business, financial condition and results of operations could be materially and adversely affected if there is any adverse change in the economic, political or social conditions in China, and in particular, the Zhejiang province and the Eastern China regions.

We rely on the experience of key executives and management personnel and our business may be severely disrupted if we lose their services

The success of our Group has been, and the future success of our Group will be, dependent on the continuing service of our management team as well as our ability to attract, motivate and retain such key personnel. In this connection, we consider that (a) Mr. Zhou, our chairman and executive Director, who has over 14 years of experience in the pharmaceutical industry and is responsible for formulation of the overall business strategy and direction of our Group; (b) Mr. Dai, our chief executive officer and executive Director, who has over 10 years of experience in pharmaceutical industry and is responsible for the overall operation of our Group's business and the overall development of sales and marketing management and strategies of our Group; and (c) Ms. Yang, our executive Director, who has over 15 years of experience in the pharmaceutical industry and is responsible for the overall procurement, quality control management of the pharmaceutical products, overall administrative and human resources function of our Group, have played a significant role in the business operations of our Group during the Track Record Period, and will continue to play a pivotal role in the future growth and success of our business. Further information about the management skills and experience of our Directors and our senior management is set out in the section headed "Directors, senior management and staff" in this document.

There can be no assurance that our Directors and our senior management will continue to perform as well as they have done in the past, and that we will be able to retain their services when their contracts expire. If any of our Directors or senior management team members is unable or unwilling to continue to serve his or her current position and we may not be able to recruit suitable replacement personnel with equivalent qualifications or talents in a timely manner, it may cause disruption to our business operation and may have an adverse impact on our ability to manage our business effectively and efficiently. As a result, it may adversely and materially affect our profitability and results of operations.

There is no assurance that we will be able to successfully pursue the strategies and this may materially and adversely affect our business, financial condition and results of operations

Failure or delay in achieving our business strategies may adversely affect us

Details of our strategies are set out in the sections headed "Business – Our business objectives and strategies" and "Business objectives and future plans – Business objectives and strategies", respectively, in this document. The successful implementation of our business plans, including, without limitation to, extending our products to the second and third tier cities to those new markets particularly in the Zhejiang province and the Eastern China regions which we have not yet explored, obtaining new product distribution rights with commercial potential and gaining a leading position in the prescription drugs segment of the pharmaceutical distribution industry, depends on a number of factors including, among others, continued growth of the pharmaceutical product market in the PRC, availability of funds, competition and change in government policies. There is no assurance that we will be able to pursue the strategies nor will any such strategies be as successful as contemplated by the management. Any failure or delay in achieving any or all of our strategies may have an adverse effect on our profitability and prospects.

Newly launched products may not be well received by the market, which could negatively affect our growth prospects

During the Track Record Period and [as at the Latest Practicable Date], we identified and acquired certain national and provincial distribution rights of products which are complementary to our existing product portfolio. Please refer to the section headed "Business – Our business model – Phase 2 – Procurement of products from our suppliers – Reduction of the reliance on our major suppliers" for details. In this connection, our growth depends, to a large extent, on whether our products introduced to the market are well received. The primary factors which may affect the acceptance of our products by the market include efficacy, quality and price of the products and the purchasing trends of our Distributor Customers and their customers. If any new product is not well received by the market because it is not as effective as competitive products or is too expensive compared to other substitutes, or for any other reason, we may not be able to recoup the investment we have made in developing such products, in which case our business, financial condition, results of operations and growth prospects may be materially and adversely affected.

Our information technology system may experience failure or breakdown and cause interruptions to our business, and failure to maintain optimal inventory levels may lead to a material adverse effect on the results of our business and operations

We have installed a centralised inventory management system to monitor and manage our inventory levels at all times. Our ability to provide customers with a timely and adequate supply of pharmaceutical products is affected by our ability to maintain proper inventories of those products. Our ability to maintain proper inventory levels at any given time is dependent on our accurate estimate of the future market demand, the supplies available from our suppliers, and the market demand for products which we hold in our inventories. Any changes in those factors could result in a shortage of inventory or overstocking of certain inventories. If we experience inventory shortages, our sales volume and relationships with customers could be materially and adversely affected. If our inventory levels are too high, we may have to write-down inventories, products may be held past expiration dates and would have to be disposed of and storage costs could increase. Either inventory shortages or excessive inventories could materially and adversely affect our business, results of operations and financial condition.

On the other hand, a failure or breakdown of any part of our information technology system may interrupt our normal business or operations, result in a slowdown in operational and management efficiency and adversely affect our ability to meet our distribution schedules. In addition, any termination of service contract with the system providers may adversely affect our business, financial condition and results of operations.

We are subject to certain risks associated with transportation and warehousing of the pharmaceutical products supplied by our suppliers for distribution to the Distributor Customers

Our suppliers deliver products from their designated warehouses located in their respective provinces in the PRC to our warehouse in Xiaoshan District, Hangzhou, PRC. Following receipt of the sales order(s) as well as confirmation and approval of delivery order(s), our logistics team commences arranging for delivery to our Distributor Customers. In view that our suppliers and the Distributor Customers are located throughout different provinces in the PRC, a reliable transportation network is crucial to delivery of the

pharmaceutical products from our suppliers to us and then from our Group to the Distributor Customers. Accordingly, any unforeseen event beyond our control such as adverse weather conditions, transportation bottlenecks, natural disasters, political disruptions or labour disputes would lead to delay in or even loss of product supply to our Group and may result in loss of revenue or claims from Distributor Customers. In addition, any poor handling during transportation by our suppliers or our logistics carriers and/or partners may damage the products and adversely affect our business operations. On the other hand, the products are stored in our temperature-controlled warehouse prior to delivery to Distributor Customers. If certain events such as fire, flooding or technical breakdown or failure of our warehouse system, we may be unable to deliver the products to Distributor Customers on schedule, which would materially and adversely damage our reputation and affect our results of operations.

Our Controlling Shareholders may exercise significant influence over us and their interests may not be aligned with the interest of the other Shareholders

Subject to the Bye-laws, the Controlling Shareholders will continue to have the ability to exercise significant influence in matters submitted to a vote of our Shareholders, including matters such as election or removal of members of our Board, the timing and amount of dividend distributions, and approval or disapproval of significant corporate transactions such as strategic investments, mergers, acquisitions, joint ventures, investments or divestitures. In fact, the interests of our Controlling Shareholders may at times differ from those of our other Shareholders. We cannot assure that our Controlling Shareholders will always take actions that will benefit our other Shareholders.

Any outbreak of communicable diseases, or occurrence of natural disasters or other catastrophic events may have a negative impact on our business

Our business operations are carried out in the PRC and we generate all the sales in the PRC with a focus in Zhejiang province. Since March 2013, various human cases of avian influenza A (H7N9) have been reported in certain regions of the PRC, including Shanghai and the provinces of Zhejiang and Anhui, where we and our major Distributor Customers are located and/or our Type 1 and 2 Distributor Customers have their respective distribution networks. There is no assurance that such communicable disease is to be adequately controlled. In addition, whether there would be any outbreak or recurrence in the PRC of severe acute respiratory syndrome, the H5N1 avian flu, the human swine flu (which is also known as influenza A (H1N1)) or any other epidemics is uncertain. Further, many major cities in the PRC are vulnerable to the threat of earthquake, flood, typhoon, drought or sandstorm. For example, an earthquake measured by the PRC's earthquake administration at magnitude 7.0 struck Ya'an city, Sichuan province on 20 April 2013, with aftershocks having continued to jolt the region subsequently. Our business is sensitive to domestic consumer demand for the products we distribute and relies on domestic labour. Any outbreak of communicable diseases, natural disasters or other catastrophic events in the PRC would adversely affect the domestic consumption, labour supply and potentially the overall GDP growth of the PRC. This may, in turn, hinder market activities and general economic growth of the PRC, and cause significant interruption to our business, which may therefore result in a negative impact on our business, financial condition, operation results and growth prospects.

We may be required to make early payment of any outstanding loans, or to increase the amount of collateral for secured borrowings (as the case may be) under the financing facilities granted during the Track Record Period and up to the Latest Practicable Date, which may adversely affect our business operation

During the Track Record Period and up to the Latest Practicable Date, we obtained (i) an unsecured loan facility on 22 November 2012 in the maximum amount of HK$18 million from a licensed money lender in Hong Kong being an Independent Third Party, which carried interest at fixed interest rate of 6% per annum and was repayable in one year from the relevant drawdown dates; (ii) an unsecured loan facility on 9 May 2013 in the maximum amount of HK$12 million from another licensed money lender in Hong Kong being an Independent Third Party, which carried interest at fixed interest rate of 6% per annum will be repayable in 6 months from the relevant drawdown dates (where we have not drawn down any amount under this facility as at the Latest Practicable Date), pursuant to which each of the lenders reserves the right to cancel such facility and to demand immediate repayment of any outstanding loan in full if any event of default occurs, for example, if interest on the loan or any other amount payable by us under the facility is not paid on the due date; and (iii) an overdraft facility of HK$5,000,000 and a revolving loan of HK$15,000,000 on 17 June 2013 with the interest rate of (a) 1.5% per annum over Dah Sing's Bank's fix deposit rate or 1% per annum over HK Inter-Bank Offered Rate, whichever is higher for the overdraft, and (b) Dah Sing Bank's HKD Prime Rate per annum for the revolving loan from Dah Sing Bank, respectively, against charge to Dah Sing Bank fixed deposit for not less than HK$5 million or its 110% equivalent in foreign currency by our Group and also corporate guarantee executed by Max Goodrich for unlimited amount. In addition, we entered into a maximum amount mortgage contract on 29 November 2012 in the maximum amount of RMB12.51 million (equivalent to approximately HK$15.55 million) with Agricultural Bank of China Limited Hangzhou Jiefang Road branch* (中國農業銀行股份有限公司杭州解放路支行) with our self-owned property located at Room 3702, Dikai International Centre, Jianggan District, Hangzhou City, Zhejiang Province, the PRC pledged as collateral (where the aggregate amount of RMB8,500,000 (equivalent to approximately HK$10,566,000) was drawn down by us as at the Latest Practicable Date for [payment of deposit to a supplier for acquisition of new distribution rights of a product] at the fixed interest rate of 6.9% per annum). Please refer to the section headed "Financial information – Liquidity and capital resources – Bank and other borrowings" for details. On one hand, we cannot assure you of non-occurrence of any event of default during the term of the loan facility in question, which will otherwise trigger the lender's exercise of the right to demand early repayment of any outstanding loan from us. On the other hand, there is no assurance that the bank may not request us in the future to increase the amount of collateral pledged for secured borrowings, particularly in case of any change in economic conditions of the PRC, which may result in any possible devaluation of the secured asset. This may result in a material adverse effect on our business, financial condition and results of operations.

Dividends declared in the past may not be indicative of our dividend policy in the future

Our Directors may declare dividends after taking into account, among other things, our results of operations, cash flows and financial condition, operating and capital requirements, the amount of distributable profits based on HKFRSs, the Bye-laws, the Companies Act, applicable laws and regulations and other factors that our Directors deem relevant. For further details of our dividend policy, please refer to the section headed "Financial information – Dividend policy" in this document. Our future declarations of dividends may or may not reflect our historical declarations of dividends and will be at the absolute discretion of our Board. There is no assurance that the amount of dividends declared by our Company in the future, if any, will be at a level comparable with that in the past.

RISKS RELATING TO THE INDUSTRY

The pharmaceutical industry is highly regulated and our business would be adversely affected if we fail to maintain our licences for sale or to comply with relevant regulations and/or our manufacturers fail to meet the requirements governing the manufacturing of those products distributed by us

Failure to comply with the applicable laws, rules or regulations could adversely affect our business and reputation

The pharmaceutical industry in the PRC is highly regulated and is subject to extensive government regulation and supervision. The PRC government has implemented certain regulatory measures and announced plans to implement additional rules and regulations for governing operation of the pharmaceutical industry. Please refer to the section headed "Regulatory Overview" of this document for a summary of the relevant laws, rules and regulations currently governing our business operations. Violation of these laws, rules and regulations may also constitute a criminal offence under certain circumstances, and could have a material adverse effect on our business and reputation, as well as our financial condition, results of operations and prospects. On the other hand, any change in compliance standards, or any new laws or regulations may prohibit us from conducting, or render it more restrictive for us to conduct our business. In this connection, we cannot assure you that we will be able to adapt to such changes, and the failure to sufficiently and promptly respond to such changes may materially and adversely affect our business, financial condition and results of operations.

We may fail to maintain or renew the relevant certificates, licences and permits necessary for operation of our business

We have obtained, among other things, (i) pharmaceutical operation permit granted by Zhejiang Province Food and Drug Administration, (ii) the business license granted by and registered with the relevant administration for industry and commerce as required by the applicable PRC laws and regulations, and (iii) the Good Supply Practices certificate granted by Zhejiang Province Food and Drug Administration. However, our existing certificates, licences and permits may be suspended or revoked or we may not be able to renew such certificates, licences and permits due to various reasons, some of which may be beyond our control, including our failure to satisfy any requirements or the standards imposed by the relevant authorities for the issue of such certificates, licences and permits, or if our products cause harmful effects to end-users or fail to comply with the registered prescription. Any suspension or revocation of, or failure to renew, our existing certificates, licences and permits could cause disruption to our business or prevent us from continuing to carry on our business.

We may be restricted or prohibited to carry out our pharmaceutical distribution business in the PRC

Our pharmaceutical distribution business is currently falling within the category of "industries in which foreign investment is permitted" under the Foreign Investment Industrial Guidance Catalog (外商投資產業指導目錄) jointly promulgated by MOFCOM and NDRC and as amended on 24 December 2011. However, we cannot give any assurance that the PRC government will continue to adopt policies which would be beneficial to our Group and/or the pharmaceutical industry in the PRC where our business operations are located, the PRC government may reduce support for healthcare services and benefits provided in China, which may bring about a decrease in demand for our services.

We may incur more costs in complying with the new laws, rules and regulations

Compliance with the new rules, regulations and measures, may increase our costs of improving the safety and credibility issues of the pharmaceutical products we distribute, which may then result in decreases in the quantities of products we sell to the customers or the price they are willing to pay for these products. This could, in turn, lower our profit margins and may have a material adverse effect on our results of operations.

Our pharmaceutical distribution operation may be affected by the regulations governing the manufacturing of pharmaceutical products distributed by us

We are only a pharmaceutical distributor, and source and procure products from the pharmaceutical manufacturers and pharmaceutical companies throughout different provinces in the PRC. Therefore, the regulations relating to the manufacturing of pharmaceutical products may affect our pharmaceutical distribution operation. Please refer to the section headed "Regulatory overview – Regulations relating to the manufacturing of pharmaceutical products distributed by us" for details of such regulations. In particular, on 17 January 2011, the Ministry of Health promulgated the current version of GMP standards (2010 revised version), which became effective on 1 March 2011, place greater emphasis on the use of effective quality control system by pharmaceutical manufacturers through the strengthening of drug manufacturing quality management systems. The enterprises which fail to meet the requirements under the 2010 revised version GMP will be prohibited from carrying out pharmaceutical manufacturing operations. In this connection, please refer to the section headed "Business – Our business model – Phase 2 – Procurement of products from our suppliers – Products shortage from our suppliers during Track Record Period" for details of the affected products and suppliers as a result of the revision of GMP standards. In the event of any inability of the pharmaceutical manufacturers and pharmaceutical companies concerned to act in compliance with the revised GMP standard or any other applicable laws rule or regulations from time to time governing the manufacturing of pharmaceutical products supplied to us for our distribution to Distributor Customers, this would severely disrupt our business and restrict us from proceeding with distribution of certain products. As a result, if we are not able to provide our Distributor Customers with products upon the terms and conditions of our respective distribution agreement or arrangements, we may face contractual claim or dispute from such Distributor Customers. This would possibly impair our relationship established with, and also our ability to retain, such Distributor Customers and hence our profitability and prospects would be materially and adversely affected.

On the other hand, there is no explicit provision in the distribution agreements with our suppliers governing the return of our paid deposits and/or prepayments (as the case may be) and/or the payment of any compensation or penalty from our suppliers to us in case of their failure to supply us quality products in compliance with all the applicable requirements regulating the manufacturing of the products we distribute (including, without limitation to, any revision of the GMP standards). In this relation, if we are unable to recover from such suppliers the entire amount (or any part) of the deposits and/or prepayments (as the case may be) paid under the distribution agreements or fail to claim any compensation whatsoever from such defaulting suppliers, our operation results and financial conditions may be adversely and materially affected.

Any actual or potential involvement in corrupt practices or other improper conduct by our Group, our employees or affiliates as well as our suppliers, Distributor Customers or ultimate customers could severely damage our reputation and have a material adverse effect on our results of business and operations

In our pharmaceutical distribution business, we are subject to the PRC laws, rules and regulations relating to healthcare fraud and abuse. As a result, we are subject to risks in relation to actions taken by us, our employees or our affiliates, or our suppliers, Distributor Customers or ultimate customers that constitute violations of the PRC anti-corruption and other related laws. There have been several instances of corrupt practices in the pharmaceutical industry, including, among other things, receipt of kickbacks, bribes or other illegal gains or benefits by pharmacies, hospitals and medical practitioners from manufacturers and distributors in connection with the prescription of pharmaceutical products. For example, a multinational pharmaceutical company in the PRC was reported in about July 2013 to be involved in an alleged bribery incident in the PRC in relation to payment of rebates and kickbacks. If we, our employees or affiliates violate these laws, rules or regulations, we could be required to pay damages or fines. In the case of our pharmaceutical distribution business, the products involved may be seized and our operations may be suspended. Any of such or similar events could therefore materially and adversely affect our business, financial condition, results of operations, reputation and prospects. Actions by the PRC regulatory authorities or the courts to provide an interpretation of the PRC laws and regulations that differs from our interpretation or to adopt additional anti-corruption laws and regulations could also require us to make changes to our operations. Our reputation and our sales activities could be adversely affected if we become the target of any negative publicity as a result of any actual or potential involvement in corrupt practices or other improper conduct by our Group, our employees or affiliates, or our suppliers, Distributor Customers or ultimate customers. Our failure to comply with these measures, or effectively manage our employees and affiliates, or monitor the daily business operations of our suppliers, Distributor Customers or ultimate customers, could have a material adverse effect on our reputation, results of operations and prospects.

The PRC pharmaceutical distribution industry is highly competitive and if we fail to compete successfully against the existence and/or emergence of alternative products and other market players our business, financial condition, results of operations and growth prospects may be negatively affected

The PRC pharmaceutical distribution industry in which we operate is highly fragmented. There were approximately 16,295 distributors in the PRC in 2012, and there were approximately 527 pharmaceutical distributors in Zhejiang province as at 19 March 2013. Fragmentation in the PRC pharmaceutical distribution market created intense competition

among the distributors. We cannot assure you that we can compete successfully in the future. If we fail to expand our customer base and secure our suppliers while maintaining the profitability to succeed in this fragmented market, our business, financial condition, results of operations and prospects may be materially and adversely affected. Our business is also subject to competition from large foreign pharmaceutical enterprises which does not only invest in the manufacture industry, but has also extended their investment to the pharmaceutical distribution and retail sales in recent years. Further, there are probably many suppliers of similar or alternative products to the products we distribute in the pharmaceutical or pharmaceutical distribution industry, and the terms of pricing offered by such suppliers may be very competitive. The availability of alternative products and changes in customers' preferences may also have an impact on the sales of our products. In this relation, we may be required to lower the pricing of our products to maintain our competitiveness. However, there is no assurance that our business and the products we distribute will remain competitive. Competition is likely to intensify if (i) the number of distributors of substitute or similar products increases due to increased market demand or increased prices; (ii) competitors drastically reduce prices due to oversupply of products; or (iii) competitors distribute new products or substitute products having comparable medicinal applications or therapeutic effects that may be used as direct substitutes for the products we distribute which are more effective with prices comparable to or lower than the products we distribute. If any of the above occurs and we fail to compete effectively in the future against the existence and/or emergence of alternative products and other market players, our business, operational results and financial conditions may be adversely affected.

Rapid changes in the pharmaceutical industry may render the products distributed by us obsolete

The pharmaceutical industry is characterised by rapid changes in technology, constant enhancement of industrial know-how and frequent emergence of new products. Future technological improvements and continual product developments in the pharmaceutical industry may render existing products distributed by us obsolete or affect our viability and competitiveness. Therefore, our future success will largely depend on our ability to (i) diversify the portfolio of products distributed by us; and (ii) source new and competitively priced pharmaceutical products which meet the requirements of the constantly changing market. If we fail to respond to this environment by sourcing new products in a timely fashion, or if future pharmaceutical products distributed by us do not achieve adequate market acceptance, our business and profitability may be materially and adversely affected.

RISKS RELATING TO THE PRC

Our subsidiaries, operations and significant assets are located in the PRC. Shareholders may not be accorded the same rights and protection that would be accorded under the Bermuda Companies Act, and it may be difficult to effect service of legal process and enforce judgments against us and our officers

Shareholders may not be accorded the same level of shareholder rights and protection that would be accorded under Bermuda Companies Act

Our Company is incorporated in Bermuda as an exempted company with limited liability. Certain of our subsidiaries and our operations are located in the PRC. Those subsidiaries are therefore subject to the relevant laws, rules and regulations in the PRC. The Companies Act may provide Shareholders with certain rights and protection of which there

may be no corresponding or similar provisions under the PRC laws. As such, investors in the Shares may or may not be accorded the same level of shareholder rights and protection that would be accorded under the Companies Act.

It may be difficult to enforce judgment and effect service of legal process in the PRC

Given the fact that we are principally engaged in the business of distributing pharmaceutical products in the PRC, substantially all of our assets are located within the PRC, and most of our executive Directors such as Mr. Zhou, Mr. Dai and Ms. Yang and other officers are residents of the PRC, whose assets may also be located in the PRC. The PRC has not entered into treaties or arrangements providing for the recognition and enforcement of judgments made by the courts in most jurisdictions. On 14 July 2006, Hong Kong and the PRC entered into the Arrangement on Reciprocal Recognition and Enforcement of Judgments in Civil and Commercial Matters by the Courts of the Mainland and of the Hong Kong Special Administrative Region Pursuant to Choice of Court Agreements Between Parties Concerned (the "**Arrangement**"), pursuant to which a party with a final court judgment rendered by a Hong Kong court requiring payment of money in a civil and commercial case according to a choice of court agreement in writing may apply for recognition and enforcement of such judgment in the PRC. Similarly, a party with a final judgment rendered by a PRC court requiring payment of money in a civil and commercial case pursuant to a choice of court agreement in writing may apply for recognition and enforcement of such judgment in Hong Kong. A choice of court agreement in writing is defined as any agreement in writing entered into between parties after the effective date of the Arrangement in which a Hong Kong court or a PRC court is expressly designated as the court having sole jurisdiction for the dispute. Therefore, it is not possible to enforce a judgment rendered by a Hong Kong court in the PRC if the parties in dispute do not agree to enter into a choice of court agreement in writing. As a result, it may be difficult or impossible for investors to effect service of process against our assets, senior management members or Directors in the PRC in order to seek recognition and enforcement for foreign judgments in the PRC.

There is uncertainty as to the application of the Circular on Strengthening the Administration of Enterprise Income Tax on Non-PRC Resident Enterprises' Share Transfers (關於加強非居民企業股權轉讓所得企業所得税管理的通知) ("SAT Circular No. 698") issued by the State Administration of Taxation, effective as of 1 January 2008

It is not certain whether or not SAT Circular No.698 is applicable on our previous equity transfer

Pursuant to SAT Circular No. 698, except for the purchase and sale of equity through a public securities market, where a non-PRC resident enterprise transfers the equity interests of a PRC resident enterprise indirectly by disposition of the equity interests of an overseas holding company ("**Indirect Transfer**"), and the overseas holding company is located in a tax jurisdiction that has an effective tax rate of less than 12.5% or does not tax foreign income of its residents, the non-PRC resident enterprise, being the transferor, should report to the competent local tax authority of the PRC resident enterprise of this Indirect Transfer. The PRC tax authority may disregard the existence of the overseas holding company if it lacks a reasonable commercial purpose and was established by abusive structuring arrangement for the purpose of avoiding the PRC tax. As a result, gains derived from such Indirect Transfer may be subject to the PRC tax to be assessed.

In April 2010, Town Health Pharmaceutical transferred its 3% interest in Max Goodrich to Mr. He. Please refer to the section headed "History and development – Corporate development and structure – Max Goodrich" for details. The transfer of the shares of Max Goodrich by Town Health Pharmaceutical may be exposed to the risk of the application of SAT Circular No. 698. However, it is uncertain whether and how SAT Circular No. 698 would apply to such equity transfer. For example, while the term "Indirect Transfer" is not clearly defined, it is understood that the relevant PRC tax authorities have jurisdiction to request information from a wide range of foreign entities. Moreover, the relevant authority has not yet promulgated any formal provisions as how to calculate the effective tax rates in foreign tax jurisdictions. In addition, there are no provisions promulgated as how to determine whether a foreign investor has adopted an abusive structuring arrangement in order to avoid PRC tax. SAT Circular No. 698 may be determined by the tax authorities to be applicable to the equity transfer transactions where non-PRC resident enterprise shareholders were involved in our history or our restructuring, if such transaction were determined by the tax authorities to lack reasonable commercial purpose.

If a competent PRC tax authority considers that it lacks reasonable commercial purpose and its establishment is an abuse structuring arrangement for the purpose of the PRC tax avoidance, it may disregard the existence of the overseas holding company. Town Health Pharmaceutical may be therefore required to pay PRC income tax regarding its gains derived from such equity transfer. Also, if SAT Circular No. 698 is eventually determined in the future to be applicable, even though our Group is neither the obliged taxpayer nor the obligatory withholder under SAT Circular No. 698 and the tax obligation remains with the transferor, i.e. Town Health Pharmaceutical, our Group is required to assist the tax authority to levy the tax. There is no provision as how to define the scope of assistance our Group shall provide and the tax authority shall have the jurisdiction to define such a broad definition. As a result, our Group may incur expense or losses to provide such assistance, or may even be exposed to the risk of the competent PRC tax authority's requirement to be responsible for such tax payment, which may amount to approximately HK$84,000.

Further, we have not made any provision for the payment of any income tax on any capital gain that may arise under SAT Circular No. 698 as it is currently unclear how the relevant PRC tax authorities will implement or enforce SAT Circular No. 698. In the event that we are required to pay the income tax on capital gain by the relevant PRC tax authorities, our tax liability may increase and our net profits and cash flow may be affected.

The fluctuation of foreign exchange rate may affect our business

The functional currency of our Group is denominated in Renminbi. During the Track Record Period [and up to the Latest Practicable Date], we raised two unsecured loans from Independent Third Parties, which were denominated in Hong Kong dollars which hence exposed our Group to foreign currency risk. On the other hand, as our financial statements are expressed in Hong Kong dollars and the exchange rate of Hong Kong dollars is pegged to US dollars, we are exposed to foreign exchange risks arising from fluctuation in Renminbi. During the Track Record Period, we recorded the exchange difference arising on translation to presentation currency of the Company of approximately HK$4,730,000, HK$1,143,000 and HK$2,354,000 for each of the two years ended 31 December 2011 and 2012 and for the six months ended 30 June 2013, respectively. As at the Latest Practicable Date, we did not maintain any hedging policy with respect to the associated exchange rate risks as the availability of hedge instruments is limited in the PRC. After [●], our accounts will be denominated in Hong Kong dollars and payment of dividends will also be denominated in

Hong Kong dollars. At present, Renminbi is not freely convertible to other currencies. There is no assurance that we will obtain sufficient foreign exchange for payment of dividends or other settlements in foreign exchange. Furthermore, our profitability may be adversely affected as a result of fluctuation in the exchange rates between the currencies in which our purchases, expenditures and sales are respectively denominated.

Inflation in the PRC could negatively affect our profitability and growth

Economic growth in the PRC has, in the past, been accompanied by periods of high inflation, and the PRC government has implemented various policies from time to time to control inflation. For example, the PRC government introduced measures in certain sectors to avoid overheating of the economy, including tighter bank lending policies and increases in bank interest rates. The effects of the stimulus measures implemented by the PRC government since the global economic crisis that unfolded in 2008 may result in an increase of inflation in the future. If such inflation occurs and is allowed to proceed without mitigating measures by the PRC government, our cost of sales would likely increase, and our profitability would be materially reduced, as there is no assurance that we would be able to pass any cost increases to our customers. If the PRC government implements new measures to control inflation, these measures may also slow economic activity and reduce demand for our products and severely decrease our growth.

Interpretation of the PRC laws and regulations involves uncertainty that could adversely affect our business and results of operations and the value of our Shares and limit the legal protection available to investors

Our pharmaceutical distribution business in the PRC is carried out through our PRC subsidiaries, and hence such business operation of our Group in the PRC is governed by the PRC legal system. The PRC legal system is based on written statutes. While prior court decisions may be cited for reference, they have limited precedential value. Since 1979, the PRC government has promulgated laws, rules and regulations dealing with economic matters, such as foreign investment, corporate organisation and governance, commerce, taxation and trade, to enhance the protections afforded to various forms of foreign investment in the PRC in general and wholly foreign-owned enterprises in particular. However, many of these laws, regulations and legal requirements are relatively new and continue to evolve, interpretation and enforcement of these laws and regulations involve significant uncertainties and different degrees of inconsistency, particularly where there is a lack of established practice available for reference. These uncertainties may limit the legal protections available to us and to investors. We cannot predict the effect of future developments in the PRC legal system, including the promulgation of new laws, changes to existing laws or the interpretation or enforcement thereof, or the pre-emption of local regulations by national laws. Any changes of such laws and regulations may materially increase our costs and regulatory exposure in complying with them. Furthermore, due to the limited volume of published cases and the non-binding nature of prior court decisions, the outcome of dispute resolution may not be as consistent or predictable as in other more developed jurisdictions, which may limit the legal protection available to us. In addition, any litigation in China may be protracted and result in substantial costs and the diversion of resources and management attention.

PRC regulations relating to acquisitions of PRC companies by foreign entities may limit our ability to acquire PRC companies and adversely affect the implementation of our strategy as well as our business and prospects

The Rules on Mergers and Acquisitions of Domestic Enterprises by Foreign Investors (2006 Revision) (關於外國投資者併購境內企業的規定) (the "**M&A Rules**"), which were promulgated in August 2006, became effective from 8 September 2006 and were amended on 22 June 2009, provide the rules with which foreign investors must comply if they are seeking to acquire a PRC company, whether through a purchase agreement with existing shareholders or through a direct subscription from a company, that would result in that company becoming a foreign-invested enterprise. The M&A Rules further require the business scope of the resultant foreign-invested enterprise to conform to the Foreign Investment Industrial Guidance Catalog (外商投資產業指導目錄). There are uncertainties as to how the M&A Rules will be interpreted or implemented. If we decide to acquire a PRC company in the future to facilitate our pursuit of future plans and implementation strategies as referred to in the section headed "Business Objectives and Future Plans" of this document for development and growth of our business, there is no assurance that we or the owners of such PRC company can successfully complete all necessary approval requirements under the M&A Rules. This may restrict our ability to implement our expansion and acquisition strategy, and could materially and adversely affect our future growth.

We may not be able to pay any dividend on the Shares given that our Company is a holding company and relies on dividend payments from its subsidiaries

We depend on the dividend payment from our operating subsidiaries in the PRC

Our Company is a holding company and a significant part of our business was carried out through our operating subsidiaries in the PRC. As a result, our ability to pay dividends depends on dividends and other distributions received from its operating subsidiaries in the PRC. If such subsidiaries incur debt or losses, it may impair their ability to pay dividends or other distributions to our Company, which could adversely affect its ability to pay dividends to the Shareholders.

Our PRC subsidiaries may not be able to make timely dividend payment pursuant to the applicable accounting standards

The PRC law requires companies, such as our subsidiaries in the PRC, to set aside part of the net profit as statutory reserves. A PRC subsidiary is required to set aside each year at least 10% of its after-tax profits for such year to the statutory reserve of such PRC subsidiary. Such reserve may not be discontinued until the accumulated amount has reached 50% of the registered capital of the PRC subsidiary. These statutory reserves are not available for distribution to our Company, except in liquidation. The calculation of distributable profits under the PRC Accounting Standards and Regulations differs in many aspects from the calculation under International Financial Reporting Standards ("**IFRSs**"). As a result, the subsidiary in the PRC may not be able to pay any dividends in a given year to our Company if it does not have distributable profits as determined under the PRC Accounting Standards and Regulations, even if it has profits for that year as determined under IFRSs.

Limitation on our PRC subsidiaries to remit dividend payment may adversely affect our business plans and hence the interests of the Shareholders

Limitations on the ability of the PRC subsidiaries to remit their entire after-tax profits to our Company in the form of dividends or other distributions could adversely affect our ability to grow, make investments that could be beneficial to our business, pay dividends and otherwise fund and conduct our business. We cannot assure that our subsidiaries will subsequently generate sufficient earnings and cash flows to pay dividends or otherwise distribute sufficient funds to us to enable us to pay dividends to the Shareholders.

Our ability to pay dividend to the Shareholders may be restricted by the terms of our agreements to be entered into with any third party in future

Restrictive covenants in bank credit facilities, joint venture agreements or other arrangements that our Company or our subsidiaries may enter into in the future may also restrict the ability of our subsidiaries to pay dividends or make distributions to our Company. These restrictions could reduce the amount of dividends or other distributions our Company receive from our subsidiaries, which would in turn restrict our ability to pay dividends to the Shareholders.

Dividends paid to our Hong Kong subsidiary might not qualify for the reduced PRC withholding tax rate under the special arrangement between Hong Kong and the PRC, and the possibility of our being classified as a "resident enterprise" of China may result in unfavorable tax consequences to us and our non-PRC shareholders under the PRC Enterprise Income Tax Law (the "EIT Law")

Payment of dividends by our PRC subsidiaries to our Hong Kong subsidiary may not qualify for the reduced PRC withholding tax rate

Our Company is incorporated under the laws of Bermuda and holds interests in our PRC operating subsidiaries. Under the EIT Law, the profits of a foreign-invested enterprise that are distributed to its immediate holding company outside the PRC are subject to a withholding tax rate of l0%. Pursuant to the Arrangement between the Mainland China and Hong Kong Special Administrative Region for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with respect to Taxes on Income (內地和香港特別行政區關於對所得避免雙重徵税和防止偷漏税的安排) effective from 8 December 2006, this rate is lowered to 5% if a Hong Kong resident enterprise owns more than 25% of the capital of the PRC enterprise distributing the dividends. However, according to the Administrative Measures for Favorable Treatment of Non-residents under Taxation Treaties (Trial) (非居民享受税收協定待遇管理辦法(試行)) issued by the State Administration of Taxation and effective from 1 October 2009, approvals from competent tax authorities are required before an enterprise can enjoy the aforesaid 5% preferential tax rate. Moreover, according to the Notice on the Issues Concerning the Application of the Dividend Clauses of Tax Agreements (國家税務總局關於執行税收協定股息條款有關問題的通知) issued by the State Administration of Taxation on 20 February 2009, if the main purpose of an offshore arrangement is to obtain preferential tax treatment, the PRC tax authorities have the discretion to adjust the preferential tax rate for which an offshore entity would otherwise be eligible. There is no assurance that the PRC tax authorities will grant approvals on the 5% withholding tax rate on dividends paid by our PRC subsidiaries and received by our Hong Kong subsidiary.

We may be classified as a "resident enterprise" of the PRC and may be therefore subject to unfavorable tax implications

Under the EIT Law and the Implementation Rules to the EIT Law, both of which became effective on 1 January 2008, an enterprise established outside of the PRC with "de facto management bodies" within the PRC is considered a "resident enterprise" and is subject to PRC enterprise income tax at the rate of 25% on its global income. If the PRC authorities were to determine that we should be treated as a PRC resident enterprise for the purpose of PRC enterprise income tax, a 25% enterprise income tax on our global income as well as PRC enterprise income tax reporting obligations could significantly increase our tax burden and materially and adversely affect our financial condition and results of operations. Although the EIT Law provides that dividend income between "qualified resident enterprises" is exempted income, it is not clear whether dividends we receive from our subsidiaries, including our Hong Kong and BVI subsidiaries, would be eligible for such exemption, if we were considered to be a PRC resident enterprise. In addition, if we are treated as a PRC resident enterprise under the EIT Law, dividends we pay on our Shares to non-PRC shareholders, and capital gains realised by such shareholders on the sale of our Shares, may be treated as PRC-sourced income. Accordingly, we may be required to withhold PRC income tax from dividends paid to non-PRC resident shareholders, and transfers of Shares by such shareholders may be subject to PRC income tax. Such tax on the income of non-resident enterprise shareholders would be imposed at a rate of 10% (or at a rate of 20% in the case of non-resident individual shareholders), subject to the provisions of any applicable tax treaty. If we are required to withhold PRC income tax on dividends payable to our non-PRC resident shareholders, or if you are required to pay PRC income tax on the transfer of the Shares, the value of your investment in our Shares may be materially and adversely affected.