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CHINA TRADITIONAL CHINESE MEDICINE HOLDINGS CO. LIMITED
中國中藥控股有限公司

(*Incorporated in Hong Kong with limited liability*)

(Stock Code: 570)

RESPONSE TO MARKET COMMENTARY

Reference is made to the announcement of China Traditional Chinese Medicine Holdings Co. Limited (the "**Company**", together with its subsidiaries, the "**Group**") dated 22 February 2019 regarding a market commentary (the "**Article**") dated 20 February 2019 made by an entity named GMT Research ("**GMT**"), in which GMT made various speculations and allegations about the changes in board composition during the past year, previous acquisitions and the financials of the Company. The board (the "**Board**") of directors of the Company (the "**Directors**") considers the Article in its entirety built on groundless assumptions, erroneous analyses and conflicting statements and is highly speculative, fabricated and misleading. The Company vigorously rebuts the Article and, in order to eradicate the false crisis created by the Article, set forth below its responses to the false allegations.

Changes in Board composition during the past year

GMT allegations:

Eight Directors and the CFO resigned over the past year without the market forewarned. "*The rush to arrange a Hong Kong roadshow in the weeks following their departure suggests the Company was caught off guard… This raises the question of whether there have been unreported issues at the Company which warrant greater oversight.*"

Company's response:

All resignations from and new appointments to the Board, including those cited in the Articles had been duly and properly disclosed by the Company in public announcements in compliance with the Rules Governing the Listing of Securities (the "**Listing Rules**") on the Main Board of The Stock Exchange of Hong Kong Limited (the "**Stock Exchange**"). As stated in the Chairman's Statement in the 2017 annual report of the Company, since its incorporation into China National Pharmaceutical Group Corporation ("**CNPGC**", together with its subsidiaries, the "**CNPGC Group**") in 2013, the Company experienced an extraordinary development from years 2013 to 2017. The compounded annual growth rate of revenue, profit attributable to owners of the Company and basic earnings per share of the Group for the past five years was 56.4%, 55.8% and 28.5%, respectively. The Company has benefited from the support of CNPGC to the Company by it nominating Directors to the Board who would meet the business needs of the Company at its different stages of development. The Group has over the years evolved into a large-scale traditional Chinese medicine ("**TCM**") enterprise with operations covering the entire TCM industry chain. With the diversity of businesses of the Group, the Board reviews its composition from time to time to ensure that combination of the experience and background of its Directors at the material time would best serve the needs of the Company for its next five year plan. In December 2018, CNPGC, as the controlling shareholder of the Company, nominated Mr. YANG Wenming, Ms. RONG Yan, Mr. YANG Binghua and Mr. WANG Kan to the Board in place of four outgoing Directors (being Mr. ZHAO Dongji, Ms. HUANG He, Mr. LIU Cunzhou and Ms. TANG Hua, and Mr. ZHAO Dongji continues to serve the Company as Vice President and Joint Company Secretary) and recommended a number of senior management members to the Company, with the view to strengthening the management capabilities of the Group in face of the rapidly developing businesses and operations. Regarding Ms. RONG Yan's subsequent resignation in February 2019 and the appointment of Ms. LI Ru to the Board in her place, Ms. RONG Yan resigned due to change of work arrangement within the CNPGC Group. Most of the newly appointed Directors and senior management have in-depth knowledge and experience in different areas in the pharmaceutical industry. The two new independent non-executive Directors appointed in February 2019, namely Mr. QIN Ling and Mr. LI Weidong, possess profound experience in their respective professions in pharmaceutical and legal fields respectively. The Company is looking forward to the guidance of the present Board, under the continued leadership of its Chairman, Mr. WU Xian, and Managing Director, Mr. WANG Xiaochun, to bring the Group to further development.

GMT claimed that the Company could not have forewarned the market about the Board changes and had rushed to arrange a Hong Kong roadshow. However, movements in board composition should be certainly considered as information that requires high confidentiality being maintained before its disclosure to the public. As part of the work of investor relationship of the Group, the Company holds regular conferences/roadshows (for events such as results announcements) and ad hoc conferences (for information such as mergers and acquisitions, major operational business developments etc.) with analysts and investors for the relevant update. However, such invester relations events would only take place after the relevant information has been disclosed to the market to ensure the relevant information is held in strict and high confidence before public disclosures. On 27 December 2018, which was the first working day after the Company had issued the announcement on Board changes on 24 December 2018, the Company held an telephone conference with analysts and investors to give an update on the changes to the Board. The Company considers that the time arrangement for such conference was appropriate in compliance with the Listing Rules requirements in corporate governance and maintence of an orderly market for the Company's securities on the Stock Exchange.

The Company unequivocally states that the Board changes that had taken place during 2018 involved no corporate governance issues.

Previous acquisitions

GMT allegations:

Tongjitang Chinese Medicines Company ("**Tongjitang**") accounted for 100% of the sales of the business of the Company, as shown in Figure 6. This was essentially a relisting exercise. The "*back-door relisting*" appears designed to minimise regulatory scrutiny.

GMT also cited two other acquisitons by the Company: 上海同濟堂藥業有限公司 (Shanghai Tongjitang Pharmaceutical Co., Ltd.*) ("**Shanghai Tongjitang**") and 貴州同濟堂藥房連鎖有限公司 (Guizhou Tongjitang Pharmcy Chain Co., Ltd.*) ("**Guizhou Tongjitang Pharmacy Chain**") in 2016.

Company's response:

As stated in the Chairman's Statement in the Company's 2013 annual report, the Group completed the acquisition of Tongjitang in October 2013 and the Group consolidated Tongjitang's financial statements starting from November 2013. It was further stated in the Chairman's Statement in the Company's 2014 annual report that FY14 was the first complete fiscal year for consolidating the financial statements of Tongjitang and its subsidiaries. Prior to the Tongjitang acquisition, the Group's revenue, gross profit and profit attributable to shareholders of the Company for FY12 amounted to RMB1,031.8 million, RMB564.0 million and RMB168.5 million respectively, while its revenue, gross profit and profit attributable to shareholders of the Company for FY13 (with consolidation of the financial statements of Tongjitang for two months only, November and December 2013) were RMB1,394.6 million, RMB825.8 million and RMB198.5 million.

It should be further noted that after completion of the Tongjitang acquisition, the enlarged Group's revenue, gross profit and profit attributable to shareholders of the Company for FY14 were RMB2,650.5 million, RMB1,643.4 million and RMB413.1 million as a result of the full year consolidation of the results of Tongjitang into the Group's financial statements. There was detailed description of the contribution of Tongjitang's business to the 2014 results of the Group in the 2014 annual report, it would be absurd for GMT to draw a statement in the Article that Tongjitang accounted for 100% of the sales of the Company for FY12 and FY13. The acquisition allowed the Group to take advantage of the high growth of Tongjitang to gain instant access to both the prescription and over-the-counter markets for orthopedics TCM finished drugs .

Although GMT gave no substantive comments on the acquisitions of Shanghai Tongjitang and Guizhou Tongjitang Pharmacy Chain, it made the causation that those transactions might have created friction between the present Managing Director, Mr. WANG Xiaochun, and his predecessor, Mr. YANG Bin and the resignation of Mr. YANG Bin and other Directors in the last two years. This comment is absolutely of no base and a sheer speculation with no substance. Nevertheless, the Board wishes to emphasise that the Company has been committed to a high level of corporate governance standard on acquisition matters. Full due diligence work is required to be carried out before proceeding with any corporate transactions and all applicable regulatory requirements (including the Listing Rules) to be duly complied with. Negotiations on any corporate transactions are conducted on an arm's length basis and handled by competent personnel of the management team, and approved by the Board before execution. The acquisitions of Tongjitang, Shanghai Tongjitang and Guizhou Tongjitang Pharmacy Chain followed the same stringent procedures and quality standards. The consideration for each of the acquisitions was determined based on market approach and with reference to price-to-earnings ratios of listed companies engaged in similar businesses, which is considered to be a commonly adopted methodology in determining consideration for acquisition of profit making companies. Details of the acquisitions were disclosed and provided to the shareholders of the Company by way of circular to shareholders or public announcement to ensure that the shareholders and market were well informed of the transactions. The acquisitions had been approved by the then shareholders or independent shareholders of the Company at general meetings (as the case may be). Shareholders who had a material interest in the transactions (if any) had abstained from voting on the relevant resolution at the relevant general meeting. In this light, the Board does not consider there were any corporate governance issues concerning the acquisitions.

Tongjitang is one of the leading pharmaceutical enterprises in the People's Republic of China (the "**PRC**") focusing on evidence-based clinical research and development of orthopedics TCM finished drugs. Benefiting from its proven clinical efficacy, Tongjitang's core products are widely used by the domestic medical institutions. Since the acquisition, sales from Tongjitang's TCM finished drugs represents about half of the Group's total sales of finished drugs. The rapid expansion of the business scale of the Company's finished drugs segment resulted from the addition of Tongjitang's products had also set a solid foundation for the acquisition of the concentrated TCM granules business in 2015. The acquisitions of Shanghai Tongjitang and Guizhou Tongjitang Pharmacy Chain in 2016 presented to the Company crucial opportunities to expand into the TCM decoction pieces with intelligent distribution centers business model, and healthcare complex businesses.

In fact, the acquisitions had marked the Company's important milestones in establishing its business development and strategic direction. To sum up, the acquisitions have enabled the Company to explicitly implement its business development strategy to become a leading TCM healthcare enterprise in the PRC.

Financials of the Group

The Board notes that the Article contains a number of analyses on the financials of the Group. Having checked the data used in the analyses, the Company finds that there is a considerable amount of inconsistent and incorrect data used in the Article, which have led to inaccurate and misleading analyses. The Board wishes to remind shareholders of the Company and potential investors to exercise extreme caution when using the information contained in the Article. Set forth below the respsonses of the Company to the allegations of GMT on the financials of the Company.

GMT Allegations:

Poor working capital cycle of 332 days in 1H18, which is in the highest 93rd percentile relative to its peer group, and has risen by 56% over the two years. GMT has calculated that the working capital cycle of 332 days in 1H18 was primarily driven by a doubling of inventory turnover days over the past three years to 272 days, and has risen by 56% over two years. The effect of the increase in inventory turnover days on the working capital cycle was partially offset by a longer payable turnover days from 50 to 94 days.

Figure 7: TCM working capital cycle (semi-annual)

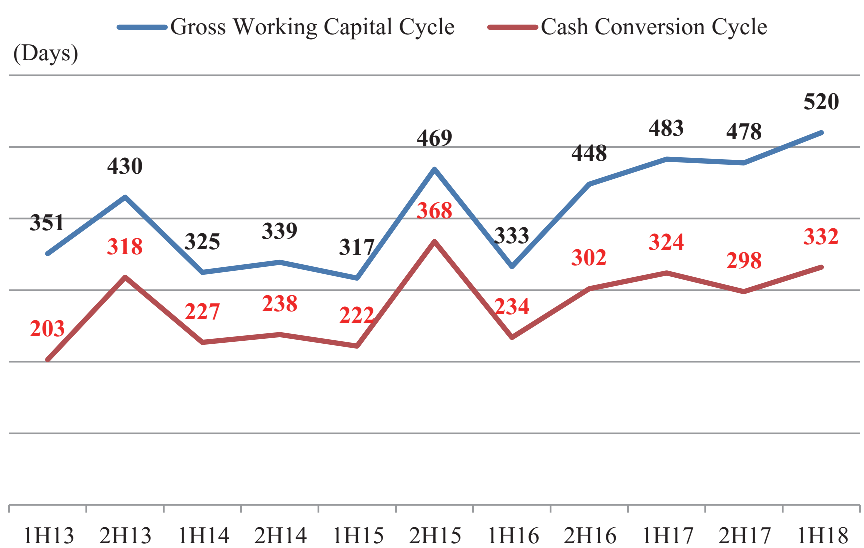
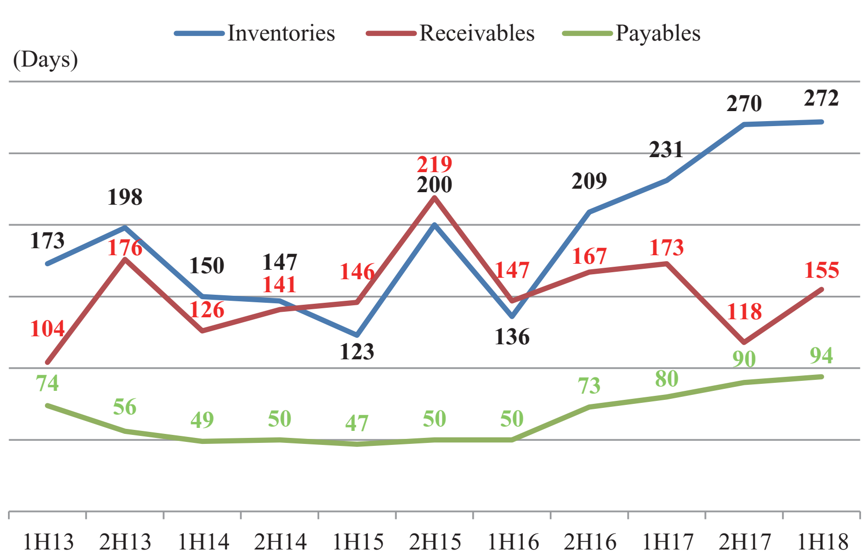


Figure 8: TCM working capital (semi-annual)



Company's response:

The Company notes that in the analysis presented by GMT, it did not use the same data source consistently to give a coherent analysis. The Company further notes that the analysis in Figure 7 and Figure 8 on working capital cycle of the Company, which contain information on the turnover days for receivables and inventories of the Group for the periods indicated above, cited source of data from Bloomberg and GMT.

However, the analysis in the Figures 10 and 11 on the receivables and inventories of the Group as reproduced below cited source of data from the Company's annual reports and GMT. It is noted that there are differences, although small (except for the receivable turnover days for 1H18, see below) in the turnover days quoted. The Company does not intend to reconcile or explain the differences noted, as it has no idea how GMT has arrived at their numbers. However, it is noted from Figures 7, 8 and 10 that there are mistakes in the comments made by GMT as follows:

(i) As depicted in Figure 7 of the Article, the working capital cycle was 332 days for 1H18, which represented an increase of 50% when compared to that of 1H15 of 222 days, or an increase of 42% when compared to that of 1H16 of 234 days. Hence, neither the comparison between the working capital cycle for 1H18 and that for 1H15 or 1H16 would suggest an increase of 56%, as stated by GMT.

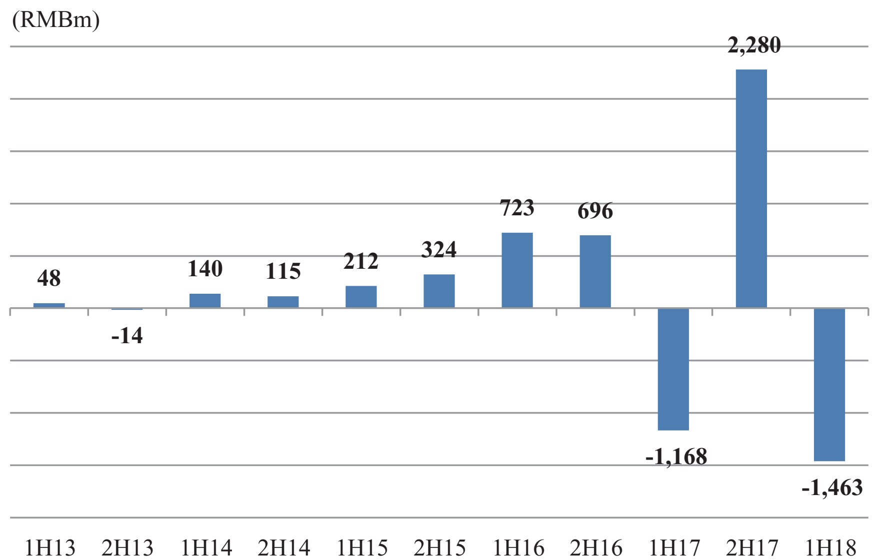
(ii) As depicted in Figure 8 of the Article, the receivable turnover days was 155 days. However, as shown in Figure 10 of the Article, the receivable turnover days quoted was 122 days.

According to the Company's calculation, there was no material change for the working capital cycle for the past two years. The working capital cycle for FY16 and FY17 were both 295 days, while the working capital cycle of 1H18 was 285 days.

GMT allegations:

Receivables balances (including trade and bills receivables) has become more volatile, falling by 32% in 1H17 to 118 days, before increasing by 31% to 155 days in 1H18, therefore resulting in increasingly large swings in operating cash flows. GMT has commented that receivable turnover days of the Company fell by 32% in 1H17 to 118 days, before increasing by 31% to 155 days in 1H18. The volatility had resulted in increasingly large swings in operating cash flows. In the Article, GMT depicted the following Figure 9 to illustrate their point:

Figure 9: TCM operating cash flows



Company's response:

The Company finds that except for the cashflow numbers quoted in respect of 1H13, 1H14, 1H15 and 1H16, all other numbers were different from the information disclosed in the financial statements of the Company. It is noted that from 2013 to now, the operating cash flow of the Group and the net profit maintained a similar increasing trend. For details, please refer to the relevant financial statements of the Company.

The Company wishes to draw the attention of the Shareholders that because of the changes in the business and operational structure, and developments in the market, subsequent to 2016, the operating cashflow of the Group for the first half and the second half of the year had seen some volatility, the principal reasons of which were as follows:

(i) following the acquisition of Jiangying Tianjiang Pharmaceutical Co., Ltd ("**Tianjiang Pharmaceutical**") in October 2015, the business of concentrated TCM granules has become the core business of the Group, accounting for approximately 67% and 66% of the turnover of the Group for FY16 and FY17 respectively. The sales of concentrated TCM granules are mainly by way of direct sales to end-user hospital customers (the "**Hospitals**"). The credit term granted to Hospitals is normally longer than the credit term granted to distributors, which are the principal customers of the Group's finished drugs products. For the purpose of shortening the time for the return of capital, and taking into account the end user customers' payment pattern in the past, the Company would normally enter into factoring activities with financial institutions for its receivables on a no recourse basis in the second half of the financial year. The factoring of the receivables would inevitably result in some fluctuations in the cash flow between the first half and the second half of the year. As the factoring activities are carried out on a rolling year-on-year basis, it does not therefore give rise to much effect on the operating cash flow of the Group on an annual basis. Therefore, the Company considers that these are proper working capital management activities in the ordinary and usual course of business of the Group.

(ii) most of the cash receipts of the Group happens in the second half of the year. The Group would normally pay off the upstream entities and Chinese medicinal herbs suppliers in the supply chain before Chinese New Year. This would also lead to fluctuation in the operating cash flow of the Group between the first half and the second half of the year. The Company considers that this is the characteristic of the pharmaceutical industry.

GMT allegations:

Deterioration in disclosure on receivable ***which were overdue but not impaired*** (emphasis added by the Company) after the change in auditor from KPMG to Deloitte in May 2016. In the Article, GMT produced a summary setting out the receivables, amounts overdue and impairment allocation of the Group from FY13 to 1H18, which is reproduced below.

Figure 10

(RMBm unless otherwise stated)	**FY13**	**FY14**	**FY15**	**FY16**	**FY17**	**1H18**
Trade and bills receivable, net	907	1,153	3,215	2,516	2,743	4,683
Trade and bills receivable, net (days)	162	142	215	160	115	122
Trade and bills receivable not impaired						
– Within 3m of invoice date	321	421	2,303			
– 3-6m after invoice date	53	84	365			
– More than 6m, less than 12m after invoice date	22	30	296			
– More than 12m after invoice date	3	10	3			
– Receivables overdue but not impaired	399	545	2,967	na	na	na
Overdue but not impaired/total receivables (%)	44	47	92	na	na	na
Impairment allowance	16	21	185	141	113	177
Impairment allowance/receivables (%)	1.8	1.8	5.7	5.6	4.1	3.8

Company's response:

The Company wishes to point out that GMT had compiled the above table using wrongly interpreted financial data. The receivables in the amount of RMB399 million and RMB545 million listed as the amounts outstanding as at 31 December 2013 and 31 December 2014 respectively represents the total trade receivables, net of allowance for doubtful debts but excluded bills receivables, as at the date indicated, not "*receivable overdue but not impaired*" as identified in Figure 10. On the same note, the ratios of 44% and 47% represented the amount of trade receivables as a percentage of the total sum of the trade and bills receivables, net, of the Company as at 31 December 2013 and 31 December 2014, respectively. And the aforesaid sums and ratios do not relate to "*trade and bills receivables overdue but not impaired*" at all.

Unfortunately and apparently, GMT did not have a correct comprehension of the financial information of the Group and had wrongly interpreted and cited the numbers in their trade and bills receivable analyses, hence the allegation that there was a deterioration in disclosure standards. Further, the Company considers it outrageous for GMT to insinuate that the change in the Company's auditors in 2016 had impacted on the quality standards of disclosure of the financial statements, without double checking their analyses before issue of such serious allegations. The Directors consider this unprofessional. Had GMT reviewed the past public disclosures of the Company, it would have known that the change of auditors in 2016 was a result of the new policy of Company to rotate its auditors after certain years of services.

The Company is assertive that the breakdown and composition of the Group's trade and bills receivables had been disclosed in details in the notes to the financial statements of the Company under "*trade and other receivables*". Shareholders may refer to the relevant sections of the annual reports of the Company for details. The Directors are of the view that the quality of the receivables are good in terms of recoverability.

There was a significant increase in the trade and other receivables account of the Group for 1H18, which was primarily attributable to the significant increases in the trade and bills receivables during the period. In the meantime, the Group has been enhancing its management over the receipt of trade and bills receivables. In the first half of 2018, compared with the year of 2015, the proportion of trade receivables aged one year or more over the balance of trade receivables were reduced by about 50%. The improvement in the ageing of the receivables has resulted in a decrease in the allowance for doubt debts as a percentage of the total account balance of trade and bills receivables.

GMT allegations:

Inventory turnovers days have been deteriorating since FY14, with a doubling of inventories turnover days over the past three years to 272 days for FY17. On the one hand, GMT made a remark in the Article that "*companies have been known to inflate profits by hiding costs in inventories, specially finished goods.*" On the other, it then followed to say that "*to assume that the Company has been capitalising costs as inventories is a worse-case scenario. It is possible that there has simply been a build-up in inventories which might require some aggressive discounting in order to clear (although, once again, this is not positive for the profit outlook).*" The payable turnover days increased from 50 to 94 days to partial offset the increase in inventory turnover days.

GMT included in the Article an analysis of the inventory balances of the Group from FY13 to 1H18 (see Figure 11 below). They have noted that the inventory turnover days had been deterioating since FY14, rising from 149 days, to 270 days by FY17. This has been driven by a build-up of finished goods, which have risen from 37 days in FY14, to 108 by FY17.

GMT mentioned that companies have been known to inflate profits by hiding costs in inventories, specifically finished goods. They further speculated that "*had the Company's finished goods remained at 14% of cost of goods sold (similar to the average of FY13 and FY14), inventories would have been around RMB870 million lower by FY17.*" However, on the next note, GMT made the remark that "*to assume that TCM has been capitalising costs as inventories is a worse-case scenario. It is possible that there has simply been a build-up in inventories which might require some aggressive discounting in order to clear (although, once again, this is not positive for the profit outlook).*"

Figure 11

(RMBm unless otherwise stated)	**FY13**	**FY14**	**FY15**	**FY16**	**FY17**	**1H18**
– Finished goods	89	115	363	803	1,383	1,711
– Raw materials/work-in-progress	316	303	873	1,091	2,169	2,392
– Inventories	**406**	**418**	**1,236**	**1,894**	**3,552**	**4,103**
– Finished goods (days)	43	37	58	78	108	110
– Raw materials/work-in-progress (days)	139	112	142	131	161	162
– Inventory (days)	**182**	**149**	**200**	**208**	**270**	**272**
Finished goods/inventories (%)	22	28	29	42	39	42
Write-down/(write-back) of inventories	5	4	6	16	(8)	5

Company's response:

Given the shift of the contributor to revenue from finished drugs to concentrated TCM granules after the acquisition of Tianjiang Pharmaceutical in October 2015, and that the inventory cycle for concentrated TCM granules is substantially different from finished drugs, the Company is of the view that the inventory analyses for FY13 to FY15 as used by GMT in the Article were irrelevant. Rather, set out below is a summary of the changes in the inventory and revenue level for FY16, FY17 and 1H18.

RMB *(million)*	**FY16**	**FY17**	**1H18**
Inventory	1,894	3,551	4,103
Inventory growth	53%	88%	16%
Revenue	6,532	8,337	5,461
Revenue growth	76%	28%	40%

As shown in the table above, the growth in inventory was lower than that in turnover for FY16 whereas the growth in inventory was much higher than that in turnover for FY17. The increase of inventory in FY17 was due to the increase in raw materials and finished goods. The increase in raw materials was attributable to the fact that (i) there was a low raw material reserve at the end of year 2016; (ii) the build-up of strategic inventory to deal with longer inspection time for quality control purpose; and (iii) the varieties of Chinese medicinal herbs procured under the centralised procurement platform increased from 105 to 211 to lower procurement costs and guarantee supply. The inventory turnover days range from 90 to 120 days for home-grown herbs, 180 to 360 days for wild herbs, and more than 360 days for rare and wild herbs. The increase in finished goods was related to concentrated TCM granules, which had inventory turnover days longer than that of TCM finished drugs.

The inventory turnover for concentrated TCM granules for 1H18 was 158 days, which was higher than that of finished drugs of 58 days. The difference was attributable to the following reasons:

(i) Concentrated TCM granules are directly sold to Hospitals: As there is no intermediate link between the Hospitals and the manufacturer, and Hospitals normally do not have large storage space, it is not expected that they will maintain a high inventory level of concentrated TCM granules. In expectation of a relatively high growth of demand of concentrated TCM granules from the Hospitals, the Company will maintain a sufficient level of inventory in more frequently use products, to ensure a steady supply and short turnaround time to the Hospitals. This steady supply has been one of the core competence of the Group in providing services to the Hospitals.

(ii) The number of products and the manufacturing cycle: It normally takes 45 days after the inspection of TCM medicinal herbs to complete a production cycle for concentrated TCM granules. There are about 200 types of commonly used concentrated TCM granules (representing approximately 80% of the sales), which has higher turnover. The Company is capable to produce about 50 to 60 types of TCM medicinal herbs simultaneously per day. The less commonly used ones are about 300 types and are produced sparcely in the year. These factors attribute to relatively longer inventory turnover days in recent years.

(iii) The reason to increase capacity: During year 2016, Guangdong Yifang's production capacity fell below demand. As a result, the inventory level of Guangdong Yifang was depleted in order to meet sales demand. In the second half of 2016, new production facilities of Guangdong Yifang commenced commercial production. The shortage in production capacity of concentrated TCM granules was by then basically resolved. In 2017, Guangdong Yifang increased its production of concentrated TCM granules finished goods.

(iv) The Company would like to point out that GMT has used a random approach to analyse the Group's costs of goods sold and profits. TCM finished drugs were the major products of the Group contributing to more than 90% of turnover in 2013 and 2014. However, the cost structure had significantly changed due to the acquisition of Tianjiang Pharmaceutical in 2015, following which concentrated TCM granules has taken over as the primary product sold and contribute to more than 60% of turnover in FY16 and FY17. It was both wrong and meaningless for GMT to use the average 2013 and 2014 finished goods to cost of goods sold ratio of 14% to deduce the cost of goods sold for FY17, without giving due consideration to the business composition of the Group at the that time.

GMT allegations:

The Company has raised "*way too much external capital relative to requirements*". It cited that the Company's net debt to equity at 31 December 2017 was just 2.4%. During 2017, the Company had a free cash inflow of HK$1.7 billion in FY17 and also raised additional debt of HK$1.2 billion. In May 2018, the Company raised a further HK$2.7 billion capital through a private placing to Ping An. They concluded that the Company has raised RMB4.2 billion surplus to requirements, even after acquisitions, between FY13 and FY17.

Company's response

The Company would like to respond that it had maintained net cash inflow from operations for the last three years to support its capital requirements on a short-term liquidity in need and payment of dividend.

As disclosed in the 2018 interim report of the Company, the Company started to built a nationwide industrial chain for TCM decoction pieces and concentrated TCM granules, which was in line with both the regional characteristics of authentic Chinese medicinal herbs resources, and with national policies for quality source tracking of decoction pieces and concentrated TCM granules. The chain also conforms with point-to-point sales strategies for TCM decoction pieces and concentrated TCM granules (localisation of production and sales).Ultimately the Group aims to establish a complete quality source tracking system for the production of Chinese medicinal herbs; exploit the scale effect of production of TCM decoction pieces and concentrated TCM granules to reduce production and logistics costs; expand market coverage and achieve a leading position in TCM decoction pieces and concentrated TCM granules industry.

For the purpose of implementing the long-term strategic development plan and optimising the Company's long-term debt structure, the Company issued two tranches of three-year notes with an aggregate principal amount of RMB4.5 billion (the "**Notes**") in 2016 and 2017 respectively to swap the bank borrowings obtained for the acquisition of concentrated TCM granules business and infrastructure construction projects for nationwide coverage.

As disclosed in the Company's announcement dated 19 March 2018, the Company introduced Ping An Life Insurance of China, Ltd. ("**Ping An**") as long-term strategic partner by way of issuance of new shares. The cooperation aimed to take advantage of Ping An's technology, platform and resources in the pharmaceutical and healthcare sector for developing the Group's TCM business. The issuance of new shares to Ping An had raised capital of about HK$2.7 billion had been mainly earmarked for the expansion of production capacity for TCM decoction pieces and concentrated TCM granules businesses and establishment of TCM industrial parks, research and development, and repayment of bank borrowings.

On 21 January 2019, the Company announced the signing of a strategic framework agreement with a subsidiary of Ping An for the establishment of a storage and trading platform for TCM raw materials. This marked the first achievement resulting from the strategic cooperation between the Company and Ping An and has set a solid foundation for the Company's future storage and trading of Chinese medicinal herbs businesses.

The relatively large cash reserve held by the Group is for (i) working capital; (ii) expansion plan for nationwide coverage of TCM business, particularly for the construction of TCM industrial parks which require substantial capital expenditures; (iii) potential investment and/or acquisition oppountities in the industry chain; and (iv) potential repayment of the first tranche of the Notes which will fall due in November 2019.

As at 30 June 2018, the Company's debt structure mainly comprised medium to long term debts. The Notes and bank borrowings repayable in more than one year had an aggregate outstanding balance of approximately RMB4.5 billion, representing approximately 88% of the Group's total debts. The Company is of the view that the Group's cash reserve is in line with the requirement of capital for its medium to long term strategic plan.

GMT allegation:

It is noted that GMT also made a remark in the Article that "*raising excess capital is a trait of companies faking their sales and hiding the fake profits in cash balances.*" However, it then went on making another remark that "*while the Company has fraud-like traits, we think it is unlikely to be faking sales.*"

Company's response:

The Company rebuts GMT's allegations against the Company on raising "*excess capital*" in that GMT has used its subjective and speculative interpretation of the financials of the Company in its financial statements. The Article is full of contradictory and ambiguous statements. The Company is of the view that the statements in the Article were factually incorrect and judgements were inferred based on erroneous presumptions about the accounting affairs of the Company, which are maliciously misleading and unacceptable.

GMT allegations:

"*The Company is highly acquisitive making nine acquisitions in 1H18 alone*", as commented by GMT in the Article. While they made the remark that complicated acquisition accounting could be used to inflate profits, they however came to the view that "*it is not immediately obvious that the Company is artificially inflating profits through acquisition accounting.*" GMT failed to give any analysis that there had been any foul play relating to the past business acquisitions by the Company but yet still included negative remark against the Company on this issue.

Company's response:

The Company considers that GMT's criticism of the Company being "highly acquisitive" is not fair. In the past five years, the Group has placed equal importance to develop its business by organic growth as well as growth by acquisition. This strategy is proven to be in the right direction, as evidenced by the impressive growth in revenue, profit and earnings per share delivered to the shareholders in the last five years as mentioned above. All acquisitions were for legitimate reasons, and have proved to have benefited the Group's performance. GMT's speculation that the Company being acquisitive could be for the reason of inflating profit through 'complicated' acquisition accounting is not logical and does not hold ground, in particular this connotation conflicts with its further statement that "it is not immediately obvious that the Company is artificially inflating profits through acquisition accounting."

The Company is of the view that the Article contains incorrect, inaccurate and misleading information and statements as well as groundless allegations and irresponsible speculations. The Company reserves its right to take legal actions against GMT.

The Board urges the shareholders of the Company and potential investors to exercise extreme caution when relying on the information contained in the Report, which might be incorrect, inaccurate and misleading.

By Order of the Board
China Traditional Chinese Medicine Holdings Co. Limited
WU Xian
Chairman

Hong Kong, 6 March 2019

As at the date of this announcement, the Board comprises twelve Directors, of which Mr. WU Xian, Mr. WANG Xiaochun and Mr. YANG Wenming are executive Directors; Mr. YANG Shanhua, Ms. LI Ru, Mr. YANG Binghua, Mr. WANG Kan and Mr. KUI Kaipin are non-executive Directors; and Mr. XIE Rong, Mr. YU Tze Shan Hailson, Mr. QIN Ling and Mr. LI Weidong are independent non-executive Directors.

* *for identification purposes*