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# 廣州藥業股份有限公司

**Guangzhou Pharmaceutical Company Limited**

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

(Stock Code: 0874)

## **CONNECTED TRANSACTION: SUBSCRIPTION OF NEW SHARES IN A NON WHOLLY-OWNED SUBSIDIARY**

On 27 August 2004, all of the Hanfang Shareholders entered into the Subscription Agreement whereby the Company conditionally agreed to subscribe for the Subscription Shares, being 44,480,000 new Hanfang Shares, at RMB1 per Share. The Subscription Shares represent about 53% of the existing registered capital of Guangzhou Hanfang and about 35% of the registered capital of Guangzhou Hanfang as enlarged by the Subscription. The Company currently holds about 54.03% interest in Guangzhou Hanfang. Immediately upon completion of the Subscription, the Company's interest in Guangzhou Hanfang will increase to about 70.04%.

The consideration of RMB1 per Subscription Share represents a premium of approximately 17.6% over the net asset value per Hanfang Share of about RMB0.85 as at 31 December 2003.

GPHL, the Company's controlling shareholder which holds about 63.26% shareholding interest in the Company, has approximately 30.78% shareholding interest in Guangzhou Hanfang. Accordingly, the Subscription which involves the Company acquiring further interest in Guangzhou Hanfang constitutes a connected transaction of the Company as defined in the respective listing rules of the Stock Exchange of Hong Kong Limited and the Shanghai Stock Exchange.

The Subscription Agreement will become effective upon approval by the Shareholders at the Company's general meeting. According to the Listing Rules, the Subscription Agreement is subject to the Independent Shareholders' approval. The Directors propose to seek the Independent Shareholders' approval of the Subscription Agreement in the EGM. GPHL and its associates will abstain from voting at the EGM in relation to the Subscription Agreement.

The Independent Board Committee will be formed to consider the Subscription and the terms of the Subscription Agreement, and an independent financial adviser will be appointed to advise the Independent Board Committee on those issues. A circular containing, among other things, details of the Subscription Agreement, the recommendation of the Independent Board Committee, the advice of its independent financial adviser and the notice of the EGM will be dispatched to the Shareholders as soon as practicable. This announcement will be published simultaneously at the Shanghai Stock Exchange.

## SUBSCRIPTION AGREEMENT

### Date

27 August 2004

### Parties

(a) *Subscriber of the Subscription Shares:*

The Company, which is one of the Hanfang Shareholders by holding about 54.03% of the existing registered capital of Guangzhou Hanfang and there is no other subscriber in the Subscription.

(b) *Other parties:*

The other 11 Hanfang Shareholders, which in aggregate hold about 45.97% of the existing registered capital of Guangzhou Hanfang. Please refer to the paragraph headed "Shareholding structure of Guangzhou Hanfang" for details of the Hanfang Shareholders. The other 11 Hanfang Shareholders have agreed to waive the pre-emptive rights to subscribe for the Subscription Shares in proportion to their existing respective shareholdings in Guangzhou Hanfang.

### The Subscription

Pursuant to the Subscription Agreement, all the Hanfang Shareholders, being the Company and the other 11 Hanfang Shareholders, have agreed to increase the registered capital of Guangzhou Hanfang by way of subscription by the Company for the Subscription Shares, being 44,480,000 new Hanfang Shares. The Subscription Shares represent about 53% of the existing registered capital of Guangzhou Hanfang and about 35% of the registered capital of Guangzhou Hanfang as enlarged by the Subscription Shares. The Company's interest in Guangzhou Hanfang will increase from the current level of 54.03% to about 70.04% as a result of the Subscription. Currently, the board of directors of Guangzhou Hanfang comprises 7 directors and the Company has appointed 4 directors to the existing board of directors of Guangzhou Hanfang. Pursuant to the Subscription Agreement, the composition of the board of directors will remain unchanged.

GPHL, the Company's controlling shareholder which holds about 63.26% shareholding interest in the Company, is a substantial shareholder of Guangzhou Hanfang by holding about 30.78% of its existing registered capital. Accordingly, the Subscription which involves the Company acquiring further interest in Guangzhou Hanfang constitutes a connected transaction of the Company as defined in the respective listing rules of the Stock Exchange of Hong Kong Limited and the Shanghai Stock Exchange.

### Consideration

The consideration for the Subscription Shares is RMB1 per Subscription Share. The total consideration in the amount of RMB 44,480,000 will be settled by the Company in cash within five business days upon the effective date of the Subscription Agreement. The total consideration will be funded by the internal resources of the Group. According to the terms of the Subscription Agreement, it will become effective upon approval by the Independent Shareholders and there is no long stop date for the Subscription. None of the conditions of the Subscription Agreement will be waivable. As at the date of this announcement, the Company has not paid any deposit for the Subscription.

The consideration of RMB1 per Subscription Share represents a premium of about 17.6% over the net asset value per Hanfang Share of about RMB0.85 as at 31 December 2003 (based on the audited net asset value of Guangzhou Hanfang of about RMB71.2 million and a total of 83,284,300 Hanfang Shares in issue as at 31 December 2003).

The terms of the Subscription Agreement, including the consideration for the Subscription Shares, were arrived at after arm's length negotiation between the Company and the other Hanfang Shareholders after taking into account (i) the factors set out in the paragraph headed "Reasons for the Subscription" below; (ii) the subscription by seven Hanfang Shareholders, being GPHL, Ms. Liu Ju Yan, Mr. Mo Shang Zhi, Mr. Cai Xing Chun, Mr. Zhao Xiang Yong and Mr. Ge Fa Huan, for Hanfang Shares in February 2003 at a consideration of RMB1 per Hanfang Share, which represented a premium of about 18.9% over the audited net asset value per Hanfang Share of approximately RMB0.841 as at 31 December 2002; (iii) the net asset value per Hanfang Share of approximately RMB0.85 as at 31 December 2003; and (iv) the nominal value of Hanfang Shares of RMB1 each. In addition, having considered the factors set out in the paragraph headed "Reasons for the Subscription" below, the Directors consider that the Subscription is in the interest of the Company and the Shareholders as a whole, and the terms of the Subscription Agreement are fair and reasonable.

## Restriction on the transfer of the Subscription Shares

The Company and Huadong Chinese Medicine, which are interested in approximately 70.04% and approximately 3.91% of the registered capital of Guangzhou Hanfang, respectively, following completion of the Subscription Agreement, are restricted from disposing of, transferring or pledging the Hanfang Shares owned by them within 3 years from the date of the Subscription Agreement, being 27 August 2004, unless otherwise agreed by all the Hanfang Shareholders. The remaining Hanfang Shareholders are not subject to such restriction on disposal, transfer or pledge of their Hanfang Shares.

The Company provides resources, other than technical know-how, and Huadong Chinese Medicine provides technical know-how for the research and development of the Chinese medicines for the Project. The Directors consider that both parties are critical for the successful implementation of the Project and continuous research and development in Chinese medicines and their production methods conducted by Guangzhou Hanfang are of strategic importance to the Group. In view of the above and in order to demonstrate commitments to the Project by the Company and Huadong Chinese Medicine, the Directors consider that the restriction on the transfer of the Subscription Shares is fair and reasonable and in the interest of the Company and the Shareholders as a whole. GPHL, through GPHL's shareholding in the Company which provides resources, other than technical know-how, to Guangzhou Hanfang. Therefore, the Directors consider that it is fair and reasonable for not to apply restriction on the transfer of its holding of Hanfang Shares. As the shareholdings of shareholders of Guangzhou Hanfang, other than the Company, Huadong Chinese Medicine and GPHL, are insignificant, the Directors consider that it is fair and reasonable for not to apply the restriction on the transfer of their respective shareholdings in Hanfang Shares.

## Completion

The Subscription is expected to be completed on the date when the new business license of Guangzhou Hanfang (reflecting its new registered capital and its new shareholding structure) is issued by 廣州市工商行政管理局 (Guangzhou Industrial and Commerce Administration Bureau). It is expected that the new business license of Guangzhou Hanfang will be issued not later than 30 business days from the date of the Independent Shareholders' approval of the Subscription.

## Shareholding structure of Guangzhou Hanfang

Set out below is the shareholding structure of Guangzhou Hanfang immediately before and after completion of the Subscription:

Hanfang Shareholders	Immediately before the completion of the Subscription		Immediately after the completion of the Subscription	
	No. of Hanfang Shares	Approximate%	No. of Hanfang Shares	Approximate%
The Company 廣州陳李濟藥廠 (Guangzhou Chen Li Ji Pharmaceutical Factory) (Note 1)	45,000,000	54.03	89,480,000	70.04
廣州中一藥業有限公司 (Guangzhou Zhongyi Pharmaceutical Co., Ltd) (Note 2)	2,000,000	2.40	2,000,000	1.57
廣州敬修堂(藥業)股份有限公司 (Guangzhou Jing Xiu Tang (Pharmaceutical) Co., Ltd) (Note 3)	1,000,000	1.20	1,000,000	0.78
廣州市醫藥工業研究所 (Guangzhou Pharmaceutical Industrial Research Institute) (Note 4)	850,000	1.02	850,000	0.67
安徽華東中藥工程集團有限責任公司 (Huadong Chinese Medicine) (Note 5)	1,150,000	1.39	1,150,000	0.90
GPHL	5,000,000	6.00	5,000,000	3.91
Ms. Liu Ju Yan (Note 6)	25,634,300	30.78	25,634,300	20.06
Mr. Mo Shang Zhi (Note 6)	600,000	0.72	600,000	0.47
Mr. Cai Xing Chun (Note 6)	550,000	0.66	550,000	0.43
Mr. Zhao Xiang Yong (Note 7)	500,000	0.60	500,000	0.39
Mr. Ge Fa Huan (Note 7)	500,000	0.60	500,000	0.39
Total	<u>83,284,300</u>	<u>100.00</u>	<u>127,764,300</u>	<u>100.00</u>

Notes:

1. 廣州陳李濟藥廠 (Guangzhou Chen Li Ji Pharmaceutical Factory) is a wholly-owned subsidiary of the Company.
2. 廣州中一藥業有限公司(Guangzhou Zhongyi Pharmaceutical Co., Ltd) is a 90.36% owned subsidiary of the Company.
3. 廣州敬修堂 (藥業) 股份有限公司 (Guangzhou Jing Xiu Tang (Pharmaceutical) Co., Ltd) is a 88.40% owned subsidiary of the Company.
4. 廣州市醫藥工業研究所 (Guangzhou Pharmaceutical Industrial Research Institute) is a wholly-owned subsidiary of GPHL and a connected person (as defined by the Listing Rules) of the Company.
5. 安徽華東中藥工程集團有限責任公司 (Huadong Chinese Medicine) is an Independent Third Party.
6. Mr. Liu Ju Yan, Mr. Mo Shang Zhi and Mr. Cai Xing Chun are the executive directors of Guangzhou Hanfang.
7. Mr. Zhao Xing Yong and Mr. Ge Fa Huan are senior management of Guangzhou Hanfang.

## **INFORMATION ON THE GROUP, GUANGZHOU HANFANG AND GPHL**

### **The Group**

The Group is principally engaged in (i) manufacture and sales of Chinese patent medicine; (ii) wholesale, retail, import and export of Western and Chinese pharmaceutical products and various medical apparatus; and (iii) research and development of natural medicine and biological medicine in the PRC.

### **Guangzhou Hanfang**

Guangzhou Hanfang commenced its business operations in 2002. Guangzhou Hanfang is a non wholly-owned subsidiary of the Company and is the main research and development arm of the Group. It is principally engaged in the research and development of Chinese patent medicine. As at 31 December 2003 and 30 June 2004, the audited net asset value and unaudited net asset value of Guangzhou Hanfang were about RMB71.2 million and about RMB71.1 million, respectively. For the year ended 31 December 2003 and the six months ended 30 June 2004, Guangzhou Hanfang recorded audited net loss of about RMB4.1 million and unaudited net loss of about RMB0.01 million, respectively.

### **GPHL**

GPHL is a state-owned enterprise in the PRC. Since its establishment in 1983, GPHL has been principally engaged in the development, manufacture and trading of pharmaceutical products.

## **REASONS FOR THE SUBSCRIPTION**

Guangzhou Hanfang is conducting research of the Project (i.e. “modernized methods for extracting the useful ingredients of Chinese medicine” (中藥提取分離過程現代化)). The useful ingredients of Chinese medicine represent the ingredients which are functionally crucial for the Chinese medicine intended to be manufactured. Guangzhou Hanfang will apply for patent for each of the products being developed by the Project. At present, the production of Chinese medicine is largely based on traditional methods, such as boiling and grinding of herbs. These traditional methods of Chinese medicine production the medicine is produced with redundant ingredients that are naturally present in the herbs, which in turn causes inconsistency in the quality of the medicine since the traditional methods of production cannot control the proportion of useful and redundant ingredients. The aim of the Project is to develop new production methods that can extract the useful ingredients from the herbs without the redundant ingredients such that the medicine produced will be of higher and consistent quality. Currently, the Project has commenced and the construction of buildings and installation of equipment for research and development and production of the products being developed by the Project has been completed. Guangzhou Hanfang has successfully developed the extraction and purification technology mainly for two Chinese medicines, namely, Ganoderma Lucidum Spore Oil (靈芝孢子油) and Feng Shi Ping Jiao Nang (風濕平膠囊). Currently, Ganoderma Lucidum Spore Oil is awaiting product certification from relevant authority of the PRC. Feng Shi Ping Jiao Nang has successfully passed the third phase of clinical testing and is awaiting product certification from relevant authority of the PRC. At present, the sales of Ganoderma Lucidum Spore Oil has commenced in Hong Kong since the second half of 2003 and Guangzhou Hanfang is in the process of applying patent for the product. The sales of Feng Shi Ping Jiao Nang has not yet commenced as the product is awaiting the product certification from relevant authority of the PRC and Guangzhou Hanfang has applied patent for the product. The sale of Feng Shi Ping Jiao Nang is expected to commence in 2005.

In view of the two Chinese medicines being successfully developed by the Project, the Directors consider that the Project can broaden the products of the Group. In addition, the Directors are of the view that continuous research and development in Chinese medicine and their production methods currently conducted by Guangzhou Hanfang at present, are of strategic importance to the Group. In order to stay competitive in the market in the long run, continuous research and development is essential for the Group. Therefore, in view of the above, the Directors consider that the Subscription strengthens the Group's ability in research and development and the Group can benefit from commercialization of the products being developed by the Project. The Directors consider that the Subscription is in the interest of the Shareholders as a whole.

Setting out below is the financial information of Guangzhou Hanfang (which is prepared in accordance with the PRC accounting standards):

	<b>As at 31 December 2002</b>	<b>As at 31 December 2003</b>	<b>As at 30 June 2004</b>
	<i>RMB'000</i> <i>(Audited)</i>	<i>RMB'000</i> <i>(Audited)</i>	<i>RMB'000</i> <i>(Unaudited)</i>
Net asset value	42,052	71,205	71,109
Loss before tax	7,123	4,130	96
Loss after tax	7,123	4,130	96

Guangzhou Hanfang recorded audited net loss of about RMB4.1 million for the year ended 31 December 2003, which represented a decrease of about 42.3% as compared with the audited net loss of about RMB7.1 million for the year ended 31 December 2002. The unaudited net loss of Guangzhou Hanfang for the six months ended 30 June 2004 amounted to about HK\$0.01 million, which represented a decrease of about 99.7% as compared with the unaudited net loss of about RMB3.6 million of the corresponding period in 2003. The Directors consider that such improvement in the financial results of Guangzhou Hanfang was mainly due to commercialization of Ganoderma Lucidum Spore Oil during the second half of 2003.

Guangzhou Hanfang intends to apply the proceeds of the Subscription for further research and development and commercialization of the products being developed by the Project.

Having considered the factors set out in this paragraph, the Directors consider that the terms of the Subscription are fair and reasonable and are under normal commercial terms. The Directors are of the opinion that the Subscription is in the interest of the Company and the Shareholders as a whole.

## **GENERAL**

GPHL, the Company's controlling shareholder which holds about 63.26% shareholding interest in the Company, is a substantial shareholder of Guangzhou Hanfang by holding about 30.78% of its existing registered capital. Accordingly, the Subscription which involves the Company acquiring further interest in Guangzhou Hanfang constitutes a connected transaction of the Company as defined in the respective listing rules of the Stock Exchange of Hong Kong Limited and the Shanghai Stock Exchange.

The Subscription Agreement will become effective upon approval by the Shareholders at the Company's general meeting. According to the Listing Rules, the Subscription Agreement is subject to the Independent Shareholders' approval. The Directors propose to seek the Independent Shareholders' approval of the Subscription Agreement at the EGM. GPHL and its associates will abstain from voting at the EGM in relation to the Subscription Agreement.

The Independent Board Committee will be formed to consider the Subscription and the terms of the Subscription Agreement, and an independent financial adviser will be appointed to advise the Independent Board Committee on those issues. A circular containing, among other things, details of the Subscription Agreement, the recommendation of the Independent Board Committee, the advice of its independent financial adviser and the notice of the EGM will be dispatched to the Shareholders as soon as practicable. This announcement will be published simultaneously at the Shanghai Stock Exchange.

## **DEFINITIONS**

In this announcement, unless the context otherwise requires, the following expressions have the following meanings:



“Board”	the board of Directors
“Company”	廣州藥業股份有限公司 (Guangzhou Pharmaceutical Company Limited), a company incorporated in the PRC the securities of which are listed on The Stock Exchange of Hong Kong Limited and the Shanghai Stock Exchange
“Directors”	the directors of the Company
“EGM”	the extraordinary general meeting of the Company to be convened consider and approve the Subscription Agreement
“Group”	the Company and its subsidiaries
“GPHL”	廣州醫藥集團有限公司 (Guangzhou Pharmaceutical Holdings Limited), a state-owned company incorporated in the PRC and the controlling shareholder of the Company which currently holds about 63.26% shareholding interest in the Company
“Guangzhou Hanfang”	廣州漢方現代中藥研究開發有限公司 (Guangzhou Hanfang Modern Chinese Medicine Research and Development Limited), a company incorporated in the PRC and currently a 54.03% owned subsidiary of the Company
“Hanfang Share(s)”	a unit (units) of RMB1 in the registered capital of Guangzhou Hanfang
“Hanfang Shareholders”	the existing shareholders of Guangzhou Hanfang, namely the Company, 廣州陳李濟藥廠 (Guangzhou Chen Li Ji Pharmaceutical Factory), 廣州中一藥業有限公司 (Guangzhou Zhongyi Pharmaceutical Co., Ltd), 廣州敬修堂(藥業)股份有限公司 (Guangzhou Jing Xiu Tang (Pharmaceutical) Co., Ltd), 廣州市醫藥工業研究所 (Guangzhou Pharmaceutical Industrial Research Institute), 安徽華東中藥工程集團有限責任公司 (Huadong Chinese Medicine), GPHL, Ms. Liu Ju Yan, Mr. Mo Shang Zhi, Mr. Cai Xing Chun, Mr. Zhao Xiang Yong and Mr. Ge Fa Huan
“Huadong Chinese Medicine”	安徽華東中藥工程集團有限責任公司 (Huadong Chinese Medicine Engineering Group Limited), a company incorporated in the PRC and an Independent Third Party
“Independent Board Committee”	the independent board committee of the Company to be formed to consider the terms of the Subscription
“Independent Shareholders”	Shareholders other than GPHL and its associates
“Independent Third Party”	an independent third party which is not connected with the Company or its subsidiaries, the Directors, chief executive or substantial shareholders of the Company and its subsidiaries or their respective associates (as defined in the Listing Rules)
“Listing Rules”	Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited
“PRC”	the People’s Republic of China
“Project”	the project to develop “modernized methods for extracting the useful ingredients of Chinese medicine” (中藥提取分離過程現代化)
“RMB”	Renminbi, the official currency of the PRC
“Shareholders”	holders of shares of RMB1 each in the capital of the Company
“Subscription”	the subscription of the Subscription Shares by the Company pursuant to the Subscription Agreement
“Subscription Agreement”	the subscription agreement dated 27 August 2004 entered into among the Hanfang Shareholders
“Subscription Shares”	44,480,000 new Hanfang Shares agreed to be subscribed by the Company pursuant to the Subscription Agreement
“%”	per cent

By order of the Board  
**He Shuhua**  
Company Secretary

Guangzhou, the PRC, 27 August 2004

*As at the date of this announcement, the Board comprises Mr. Cai Zhixiang, Mr. Zhou Yuejin, Mr. Feng Zansheng as executive directors, and Mr. Wu Zhang, Mr. Wong Hin Wing and Mr. Zhang Heyong as independent non-executive directors.*

Please also refer to the published version of this announcement in The Standard / Hong Kong Economic Times.