
Response to Query on Financial Statements and Dividend Announcement for the 12 months ended 31 December 2019 (“Results Announcement”)

The Board of Directors of Pharmesis International Ltd. (**“Company”** together with its subsidiaries, collectively the **“Group”**) wishes to provide the following information in response to the queries from Singapore Exchange Securities Trading Limited (**“SGX-ST”**) on 9 March 2020.

We refer to the Company's FY2019 results dated 27 Feb 2020 for the financial year ended 31 Dec 2019 (**“FY2019”**). Please provide clarification on the following:

SGX's Query

- 1) Please provide a breakdown and disclose the reasons why "selling & distribution costs" decreased by only 9.5% when revenue decreased a significant 42.2% in FY2019.

Company's response:

In FY2019, revenue from prescribed drugs decreased by RMB 3.0 million and revenue from non-prescribed drugs/distribution segment decreased by RMB 24.1 million mainly due to lower revenue from Er Ding products. The sales of non-prescribed drugs were mainly through distributors which the selling and distribution costs were lower as compared to sales of prescribed drugs. Hence, the selling and distribution costs decrease by 9.5% when revenue decreased a significant 42.2% in FY2019. Selling and distribution costs comprised personnel expense, advertising costs, travelling expense and delivery expense.

SGX's Query

- 2) Please also disclose the reasons for the increase in "administrative costs" of 33% when revenue in fact decreased by 42.2% in FY2019.

Company's response:

Administrative costs increased by RMB 3.1 million or 33.0% from RMB 9.5 million in FY 2018 to RMB 12.6 million in FY 2019 mainly due to the RMB 1.2 million losses incurred following temporary closure of Longlife's plant as a result of severe flooding in September 2019, RMB0.1 million allowance for stock obsolescence, RMB0.3 million increase in contribution to China's Disabled Persons' Employment Security Fund, RMB0.2 million fines and RMB 1.0 million write-back of allowance for doubtful debts in FY 2018.

SGX's Query

3) Please provide a breakdown of the administrative costs of RMB 12.6million.

Company's response:

<u>RMB million</u>	<u>FY2019</u>	<u>FY2018</u>	<u>Variance</u>
Main admin expenses (salaries, audit fees, listing exp, professional fees etc)	9.5	9.2	0.3
Fines	0.2	0.0	0.2
Social insurance expense	1.6	1.3	0.3
Allowance for stock obsolescence	0.1	0.0	0.1
Write back of impairment loss on trade receivables	0.0	(1.0)	1.0
Losses incurred following temporary closure of Longlife's plant as a result of severe flooding in September 2019	1.2	0.0	1.2
Total Administrative costs	12.6	9.5	3.1

SGX's Query

- 4) For the 12 months' ended 31 Dec 2019, government grants decreased by 98.9%.
- Please disclose the reasons for the 98.9% decrease in government grants.
 - As previously grants were given due to growth and research as disclosed by the Company previously, does this reflect the Company's loss of competitiveness?
 - Please disclose what are the Group's plans for growth moving forward.

Company's response:

- Every year, the government will roll out different grants for different objectives, scope and projects etc. The nature of government grants are usually one-time and non-recurring. The group did not secure as much government grants in FY2019 as compared to FY2018 and this resulted in the 98.9% decrease in government grants.
- As mentioned above, grants were non-recurring in nature and given to companies based on many factors. This does not reflect the Company's loss of competitiveness in any ways.
- The Group's plans for growth moving forward are to focus on exploring ways to improve sales, managing the operations cost-effectively and research & development activities with the aim of producing new products.

SGX's Query

- 5) In the 3 months' ended 31 Dec 2019, the Group recorded an impairment loss of RMB 6.1million on construction-in-progress.
- Please elaborate on and provide details of this "impairment loss on construction-in-progress" of RMB 6.1million;
 - To provide details on the progress and size of the Jiangyou's construction.
 - Please elaborate on the reasons why Jiangyou's construction-in-progress has to be impaired and how the RMB6.1million was derived;
 - What is the basis for the impairment amount?

Company's response:

The newly implemented purchase-with-target-quantity in "4+7" cities policy by the PRC government since the end of 2018, has caused a huge decrease in drug prices and intense price wars between pharmaceutical companies. This latest unforeseen policy has resulted in the current challenging market conditions. In view of the above which has resulted in significant decrease in the sales and prices of our Er Ding products, the management has decided that it is in the best interest of the group to delay the completion of the construction of the Jiangyou production facility until market conditions improve.

As at 31 December 2019, the carrying value of Jiangyou's construction-in-progress ("CIP") was RMB 33.9 million. In accordance with Singapore Financial Reporting Framework (International), non-financial assets are assessed for impairments at each statement of financial position date. Based on the valuations obtained from an independent valuer, the fair value of Jiangyou's CIP, was lower than the carrying value by RMB 6.1million. As a result, the Group recorded an impairment loss of RMB 6.1million on Jiangyou's CIP.

SGX's Query

6) As at 31 Dec 2019, the Group recorded "accrued liabilities and other payables" of RMB 12.2million.

- a. Please provide a breakdown and disclose what are these accrued liabilities and other payables;
- b. Please explain the reasons for the material items and the approximately RMB 3million increase in "accrued liabilities and other payables" when revenue in FY2019 significantly decreased by approximately RMB27 million

Company's response:

- a. The breakdown is as follows:

<u>RMB million</u>	<u>FY2019</u>	<u>FY2018</u>	<u>Variance</u>
Other payables	10.3	8.2	2.1
Accruals	1.3	0.9	0.4
VAT payable	0.4	0.6	-0.2
Advances from customers	0.2	0.2	0.0
Total Other payables and accrued liabilities	12.2	9.9	2.3

- b. The RMB 3million increase in other payables was mainly due to amount payables to creditors which contributed to the increase in Jiangyou's construction-in-progress.

SGX's Query

7) At para 1(b)(ii), the Company disclosed that its bank borrowings are secured over the land use rights and buildings of a subsidiary. Please disclose the assets over which the bank borrowings are secured.

Company's response:

The bank borrowings are secured over the land use rights and buildings (production facilities in Gulin) of the subsidiary, Sichuan Longlife Pharmaceutical Co., Ltd.

SGX's Query

8) At para 1(c), the Company disclosed an "acquisition of non-controlling interest" of RMB 15.7million in FY2019. Please disclose what the "acquisition of non-controlling interest" of RMB 15.7million refers to. Please confirm if the Company has complied with Listing Rule 706A read with Listing Rule 704(17).

Company's response:

At para 1(c), the "acquisition of non-controlling interest" of RMB 15.7million refers to the acquisition of 30% of the equity interest in Sichuan Longlife. The acquisition was approved by shareholders at the Extraordinary General Meeting of the Company held on 26 April 2019. The Company confirmed that it has complied with Listing Rule 706A read with Listing Rule 704(17).

SGX's Query

9) At page 10, in its report on its "Full Year Ended 31 December 2019", the Company disclosed that "Administrative costs increased by RMB 3.1 million or 33% from RMB 9.5million in FY 2018 to RMB 12.6million in FY2019 mainly due to the RMB 1.2million losses incurred...". please disclose the breakdown for this RMB 1.2million losses for the temporary closure of Longlife's plant in Sep 2019.

Company's response:

The RMB 1.2million losses for the temporary closure of Longlife's plant in Sep 2019 comprise RMB0.5 million personnel expenses and RMB 0.7 million manufacturing costs.

SGX's Query

- 10) In FY2019, "allowance for stock obsolescence" amounted to "RMB0.1 million" and RMB0.8million of inventories were written off.
- Please explain why the RMB 0.1 million allowance for stock obsolesces in administrative expenses and the RMB 0.8million in inventories written off" were reported under "operating costs".
 - To elaborate the nature of each of the types of impairment and also explain why these are classified as "administrative expenses" and as "operating cost" respectively.

Company's response:

- The nature of other costs were one-off and non-recurring. The RMB 0.8million in inventories written off were reported under "other costs" as and the inventories written off were due to the flooding at Longlife's plant, which was one-off and non - recurring in nature. The RMB 0.1 million allowance for stock obsolesces were classified in administrative expenses as per previous years' classification.
- The nature of other costs were one-off and non-recurring. Other costs of RMB 7.9 million in FY 2019 were RMB 0.5 million impairment loss on right-of-use assets, RMB 6.1 million impairment loss on construction-in-progress, RMB 0.5 million impairment loss on property, plant & equipment and RMB 0.8 million inventories written off. Impairment losses were classified in other costs because they were one-off and non -recurring in nature and as per previous years' classification.

BY ORDER OF THE BOARD

Wu Xuedan
Executive Director and Chief Executive Officer
11 March 2020