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Latest Comments

"What we've seen is pharmaceutical firms shifting the direction of their pipelines, getting away from the mass blockbusters and going more toward niche indications like cancer, neurology, immunology. These are areas where the amount of patients is smaller, but the pricing point for these drugs is much higher, so you can still have a blockbuster new drug, but it's a different type of model."

Damien Conover
Morningstar

"In this economic environment, patients are looking to save more. So there has been some impact on prescriptions. Certainly, the reimbursement world has changed and for pharmaceuticals not for the better. Those kinds of headwinds are largely reflected in the share prices of the companies. It is a big, overarching issue in terms of the multiples that these companies trade at."

David Amsellem
Piper Jaffray

"Over the next couple of years, as the carriers begin to roll out 4G wireless, particularly LTE networks, which Verizon and AT&T plan on doing over the course of the next few years, that could present an opportunity for some organic growth. That has the potential at least to be a transformational technology for the industry. But on a consolidated basis, we're several years away from any material impact to consolidated financial results as a result of 4G wireless."

Christopher C. King
Stifel Nicolaus

Pharmaceuticals

Analyst Interviews

The health care reform plans currently being formulated in Congress have a lot of potential to change the space for pharmaceutical companies, according to Damien Conover of Morningstar. He expects increased volumes of drugs as more people become insured, but also concessions on pricing by the pharma companies. He sees potential upside notwithstanding because the higher volumes should more than offset the $80 billion of cost that the companies will have to spend. He sees better growth in this sector longer-term and he thinks the patent expiration issue will be somewhat offset by emerging countries which are starting to demand more branded drugs. David Amsellem of Piper Jaffray focuses on smaller cap specialty pharma companies, favoring those with significant brand business and those that have managed their product life cycles well. They have the ability to sustain cash flow growth, either through development or acquisition, even after key top-line divers have seen their patents expire. For specialty pharma, the goal for companies is to continually find ways to reinvent themselves. That is the challenge and it is a main reason why the multiples for these firms typically trade closer to big pharma than they do to big biotech. Mumbai-based Prashant Nair of Citi Investment Research mostly covers smaller Indian pharma companies that have gained growth and traction in market share as they compete against the large US firms. Going forward, he sees a lot of opportunities in the Indian market as companies continue to form alliances with large cap names and fill in the pipeline gaps of some large generic and pharma companies.

Telecommunications/Services & Equipment

Analyst Interviews

The telecom services sector has been out of favor for most of this year. It is viewed as a late cyclical or defensive industry, which typically does not perform well in a recovering economic climate. Michael Nelson of Soleil Securities covers two subsectors, wireless and the rural local exchange sectors (RLECS). He sees the Latin American market for wireless as under-penetrated with opportunity for high growth. The RLECs are a good defensive investment choice with an attractive dividend yield that limits downside risk. Chandan Sarkar of Auriga USA points out a clear difference between the carriers and the equipment vendors, contrasting the carriers' pressures from increased competition and the poor economy with the equipment vendors potential for future consolidation. He also touches on the net neutrality battle taking place between the Bells, cable MSOs and new players like Apple and Google. Christopher C. King of Stifel Nicolaus sees the US as a more mature telecom market with very little near-term organic growth opportunities. He is focusing more on the emerging market names in telecom.

China Sky One Medical, Inc. (CSKI)

YAN-QING LIU, Founder, Chairman and CEO of China Sky One Medical, Inc., is Chief Executive Officer, President and Director of Harbin Tian Di Ren Medical Science and Technology Company (TDR); he also serves as General Manager of CSKI's Harbin Bio-Engineering subsidiary. Mr. Liu graduated from the Prophylactic Department of Harbin Medicine University, where he obtained his bachelor's degree. In 2005 he studied at Tsing Hua University and earned an executive master's of business. Before establishing his own company, he gained eight years of experience as a reporter at *Family Health Newspaper*, and he has over 10 years of experience in drug marketing, research and development of new drugs, and enterprise management. Mr. Liu has been instrumental in establishing TDR's sales program and sales network covering the PRC.

STANLEY HAO is the Chief Financial Officer of China Sky One Medical, Inc., a position he's held since November 2008. Mr. Hao was also recently appointed board secretary of CSKI in June 2008. From January 2006 through June 2008, Mr. Hao served as the President's Assistant and Financial Officer for Sumitomo Group Canadian Branch, an integrated trading company. Prior to this, Mr. Hao served as Marketing Executive and Canadian Market Analyst for MGM Mirage, an entertainment company that owns and operates casino properties. From September 1997 to September 2004, Mr. Hao was Chief Executive Officer and Co-founder of SunnyZone Consulting Co. Ltd., a financial consulting company. Mr. Hao holds bachelor's degrees in economics and arts from Beijing University Union and an MBA from the University of Phoenix.

SECTOR — PHARMACEUTICALS

(ANG613) TWST: Let's begin with a brief historical sketch of China Sky One Medical and a summary of the things the company is doing at the present time.

Mr. Hao: China Sky One Medical, Inc., is located in Harbin, which is in the northeast of China. The company specializes in the manufacture of traditional Chinese medicines (TCMs), Western medicines and bioengineered products, which include biological drugs and testing kits used to detect and treat a variety of diseases. We are one of the few Chinese pharmaceutical companies in China with an extensive national distribution network, a diverse product portfolio based on our proprietary intellectual property, a state-of-the-art R&D center with a pipeline of new products and an experienced management team with deep industry knowledge. The company reported revenues of $57 million in the first half of 2009, an increase of 57.6% versus the same period last year. Net income for the first six months of 2009 reached $16.7 million, or $1.01 per diluted share, compared to $12.0 million, or $0.78 per diluted share, for the same period of 2008.

China Sky One Medical has four subsidiaries. Three of them are engaged in manufacturing traditional Chinese medicines and one, Harbin First Bioengineering, is engaged in the manufacture of bioengineered products. The company upgraded to the American Stock Exchange in May 2008 and then upgraded to the NASDAQ Global Market in September 2008. This provided a much more liquid market for our stock.

TWST: Are your products directed primarily at weight loss or general health?

Mr. Hao: While our Sumei Slim Patch for weight loss is one of our leading products, we have a very broad product portfolio. The pharmaceuticals that we manufacture treat illnesses in major disease categories, ranging from cardiovascular, pulmonary and central nervous system diseases, but also include remedies for many common ailments such as colds, fevers, and coughs and toothaches. We currently manufacture 89 products in a variety of deliveries and forms, such as medicated patches, suppositories, sprays, ointments, capsules, injections and diagnostic kits, which can diagnose fatal illnesses such as heart and kidney disease in early stage. Though the weight loss product you mentioned is one of our top-selling products, accounting for 18% of total revenue in 2008, it is only one of our products. As I mentioned, our pharmaceuticals treat a wide variety of common diseases. In the near term, we are focused on developing and further marketing our TCM products for common disease, as well as our biological testing kits. We believe that high

Such health products such as these will make a major contribution to our revenues in the long run.

TWST: Would you give us some sense of the scientific basis for what you do?

Mr. Hao: We have been expanding our R&D efforts to increase our portfolio of proprietary products and are currently building a new state-of-the-art research center. The company has a 25-person R&D team. In terms of R&D, our focus is on clinical medicines for first-line disease treatment as well as antibiotics that treat infections. We are also involved in stem cell research and are working to develop cord stem cell banks, an area that we believe holds great opportunity for future growth. We also apply our R&D efforts to traditional Chinese medicines, which have been used in China for thousands of years to treat all kinds of illnesses. Modern Chinese traditional medicines are made in different ways now and have new forms of delivery, whereas traditionally there was a bunch of different grasses put in a pot and stewed for 24 hours to get a yellow watery drink. Modern Chinese traditional medicines are made in a way similar to Western medicines. And through our R&D effort, we are able to improve not only the delivery of TCM products but their effectiveness, making sure that they are more easily absorbed into the human body. For example, our Slim Patch, which is made from extractions of five different traditional Chinese ingredients, is applied around the belly button. And through penetration, it can stimulate the digestion system and adjust hormones, especially in women. Our bioengineering R&D team has also developed and continues developing diagnostic kits that are able to track biomarkers of a variety of fatal disease, such as cardiac arrest, breast cancer and AIDS.

TWST: Would you tell us how you work with distributors? How do you distribute your products?

Mr. Hao: We engage our sales through partnerships as well as our own sales force. We have an extensive distribution network that covers 24 provinces in the PRC. We continue to refine our distribution strategy, which is comprised of locating more regional agents as well as our in-house sales force that is stationed within pharmacies to promote our own products. This gives us a unique advantage among our competitors and allows us to increase our sales efficiency.

We have steadily expanded and built up our distribution network since 2007 and have also signed distribution agreements with major pharmacy chains, such as Netstar, TongRenTang and other distributors, such as Shaanxi Xintai Pharmaceutical Company, for several of our patch products. Exclusive agreements with leading distributors such as these allows us to tap into an extensive network in local markets, and help us sell and market our products nationwide. In addition, we can give them favorable prices and monitor inventory turnover.

TWST: Who would you say are China Sky One's nearest competitors? What gives you an advantage over your competitors?

Mr. Hao: The Chinese pharmaceutical market is massive and still has huge potential, even though there are already many players. To address our major competitors, we would have to break down our products individually, and for each product we might have hundreds of major competitors in the China Mainland market. So this question might be narrowed down to some of our major competitors on our top-selling products. For example, we manufacture and sell Compound Camphor Cream and other creams to treat all sorts of skin diseases. The major competitors are Janssen and 999 Pharmaceuticals. These pharmaceutical enterprises are very reputable in China, and the competition between China Sky One and these two pharmaceutical concerns is running red hot. However, we believe that through our market and advertisement efforts, we can be the leading player in this market in three years from now.

"I don't think that a lot of investors in the United States truly understand the significance of traditional Chinese medicines in China. In Mainland China and throughout East Asia, TCMs are accepted as mainstream medical care and are widely preferred among the general population although they are considered to be 'alternative' medicines in the Western world."

TWST: What are the government regulations that cover China Sky's products?

Mr. Hao: The Chinese government has championed medical reform, and not long ago it issued the first version of the the National Basic Medicine Catalogue. Within the 307 pharmaceutical products, we have seven products not often seen among Chinese pharmaceutical manufacturers. Chinese medical reform will benefit the pharmaceutical industry in general as Chinese citizens spend more on pharmaceuticals and health care, which will receive a higher percentage of reimbursements from either local or the federal China government. In addition, it is expected that more retail pharmacies will be covered in more rural areas of China as a result of the reform, and that retail pharmacies' distribution channels will be extended. Similar to what we have done with distributors in metropolitan areas, we have now initiated collaboration with sales agents who are specialized in rural markets in China. We plan to focus on this market going forward.

The basic medicine catalogue, it includes very basic products that treat common diseases. However, it won't be very meaningful to the revenue growth of a company by having many products included in this list. The key is that a company should have very good and proprietary products that are able to sustain consumers' interests and generate growing sales. In addition, the distribution channels and marketing strategies are crucial.

TWST: Last month the company announced plans to distribute its patches in Canada. Will there be future moves into international markets?

Mr. Hao: This question has been asked by a lot of our U.S. shareholders. Sales overseas for China Sky One Medical's products have been lower than domestic sales. Exports accounted for less than 10% of 2008 revenues. In order to have more of a presence in North America so that our U.S. shareholders may have a better understanding of our products, we will have to put more effort into the North American market. We have exported 40,000 units of our pain relief patch through our Canadian distributor. Shortly after, during a roadshow in Los Angeles in the middle of September, we signed another distribution agreement with a distributor in Los

Angeles for our Slim Patch product. So, yes, the answer is that it is positive that we plan to promote more sales overseas, although we all have a clear vision that the growth in the near future is still located in China. However, we plan to continue opening up overseas markets so that our products can be circulated in the United States and in European countries. We are currently applying for the CE certification to access European markets.

TWST: As far as your growth potential over the next few years, will international acquisitions play a part?

Mr. Hao: Acquisitions, whether domestic or international, are definitely one of the fastest ways for the company to grow, as long as the acquisition in question provides us the right products, equipment, sales channels and technology or patents that generate synergy with the current business. China Sky One has been searching for potential acquisition targets according to the standards I just mentioned. To date, we haven't yet identified a final candidate for our next acquisition, nor have we developed a clear acquisition schedule.

TWST: Do you see any trends that might work against the company? Is there competition that might challenge you? Are there internal issues within the company that remain to be worked out?

Mr. Hao: Intense competition in the market could put more pressure on selling prices. Although we never want to be involved in a price war, market competition in China is fierce at the moment and there are a lot of players in the pharmaceutical market, which can put pressure on our gross margins. Cost of goods sold could also rise due to inflation in China. As a result, we don't expect to see a high percentage increase in gross profit in the near future. In addition, our operating expenses will also increase due to several factors. First, our research and development investment will increase in terms of percentage of revenue. In 2008 R&D expenditures were around 8% of total revenue, and this is expected to increase to 10-12% in 2009. In addition, marketing and advertising is another growing expenditure, and in China it is extremely important — probably more so than in any where else in the world — to have a large and effective marketing and advertisement campaign. So through these above accounting points, we expect that our net profit will not increase in a high percentage comparing with the year of 2008.

TWST: Are you confident the current management team has the players in place to navigate through these areas and keep the company on the right track?

Mr. Hao: We have a strong management team with deep industry experience led by our Chairman and President, Yan-qing Liu, who holds a bachelor's degree from Harbin Medical University and an executive master's of business from Tsing Hua University. He is a visionary when it comes to the pharmaceutical industry in China and has successfully navigated our strategic acquisitions and distribution agreements. In addition, Ms. Xaio-yan Han has served as General Manager of our wholly owned Harbin Tian Di Ren Medical Science and Technology Company (TDR) and received an MBA from Harbin Industrial University. Also we recently strengthened our board with the appointment of Mr. William Wei, who has over 15 years of experience in financial services and government relations, including investments, joint ventures, mergers and acquisitions, and management consulting.

TWST: What barriers do you confront when you describe China Sky and its activities or strategies to the investment community? Are there any misperceptions you encounter on a regular basis?

Mr. Liu: As Mr. Liu mentioned, China Sky One has just been in the U.S. capital market for a couple of years. I don't think that a lot of investors in the United States truly understand the significance of traditional Chinese medicines in China. In Mainland China and throughout East Asia, TCMs are accepted as mainstream medical care and are widely preferred among the general population although they are considered to be alternative medicines in the Western world. In addition, TCMs are heavily subsidized by the Chinese government unlike Western medicines. As a result, the operating environment and business culture for pharmaceutical companies in China are significantly different than the pharmaceutical companies in the U.S. The company will continue improving at many fronts to inform investors and communicate with them effectively. We believe that the best way to address misperceptions is that the company can continue delivering strong performance financially and operationally.

"Modern Chinese traditional medicines are made in a way similar to Western medicines. And through our R&D effort, we are able to improve not only the delivery of TCM products but their effectiveness, making sure that they are more easily absorbed into the human body."

TWST: What would you reasonably expect CSKI to look like in about three years?

Mr. Liu: In the external-use TCM drug market, we expect China Sky One to be ranked among the top three players in China over the next three years. In terms of our diagnostic testing kits and biological products, we expect to become one of the leading manufactures in China.

TWST: What would be the two or three best reasons for the long-term investor to look closely at CSKI as an investment today?

Mr. Liu: One reason why current and potential shareholders should pay more attention to China Sky One is that it is more attractively valued relative to its peers, and has achieved significant growth in revenues and earnings with strong cash flows from operations. We expect our product portfolio to continue to perform well, underpinned by solid industry fundamentals for the pharmaceutical industry in China. Our extensive distribution channel, strong portfolio of existing and new products, and the vision and experience of our management team should also give investors confidence in our future growth. In addition, we believe that projects such as the development of cord stem cell banks have the potential to be future blockbusters. China Sky One Medical has the exclusive rights to stem cell banks in Heilongjiang province. Each year there are roughly 500,000 newborn babies in Heilongjiang province alone. For each baby, there will be an entrance fee as well as a yearly maintenance fee. Calculating the future cash flow from this project can be very exciting. We continue to invest in this project and believe it can fuel another significant growth for our company in the future.

TWST: What have I overlooked? Are there any thoughts or issues that you would like to address?

Mr. Liu: The strength of our intellectual property provides a key competitive advantage that significantly improves our ability to generate revenue. In fact, many of our peers don't have the intellectual property that is needed to produce leading pharmaceutical products such as ours and instead rely on imitating others. Our biological diagnostic kits employ the latest technologies nationwide and even worldwide. We have a number of other products in our R&D pipeline that can be future blockbusters. My last point would be that our unique distribution channel compared to other pharmaceutical companies and strong management teams should give confidence to our shareholders.

TWST: Thank you. (KL)

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