LATTICE SEMICONDUCTOR CORP
Form 10-K/A
November 14, 2014
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-K/A

(Amendment No. 1)
(Mark One)

[X] ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE FISCAL YEAR ENDED DECEMBER 28, 2013

or

o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

FOR THE TRANSITION PERIOD FROM TO
Commission file number: 000-18032

_____

LATTICE SEMICONDUCTOR CORPORATION
(Exact name of registrant as specified in its charter)

Delaware	93-0835214
(State of Incorporation)	(I.R.S. Employer Identification Number)
5555 NE Moore Court	
Hillsboro, Oregon	97124-6421
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code: (503) 268-8000
Securities registered pursuant to Section 12(b) of the Act:

_____

(Title of Class)	(Name of each exchange on which registered)
Common Stock, $.01 par value	NASDAQ Global Select Market

Securities registered pursuant to Section 12(g) of the Act: None
Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes o No [X]
Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.
Yes o No [X]
Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes [X] No o
Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes [X] No o
Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§229.405 of this chapter) is not contained herein, and will not be contained, to the best of the registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this

Form 10-K. [X]

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of “large accelerated filer”, “accelerated filer”, and “smaller reporting company” in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer o	Accelerated filer [X]
Non-accelerated filer o	Smaller reporting company o

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes o No [X]

Aggregate market value of voting stock held by non-affiliates of the registrant as of June 28, 2013	330,493,725
Number of shares of common stock outstanding as of November 11, 2014	118,033,629

DOCUMENTS INCORPORATED BY REFERENCE

The information required by Part III of this Report, to the extent not set forth herein, is incorporated herein by reference from the registrant's definitive proxy statement relating to the 2014 Annual Meeting of Stockholders, which definitive proxy statement was filed with the Securities and Exchange Commission on March 20, 2014.

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EXPLANATORY NOTE

Lattice Semiconductor Corporation (“Lattice” or the “Company”) is filing this Amendment No. 1 on Form 10-K/A to amend its Annual Report on Form 10-K for the year ended December 28, 2013, filed with the Securities and Exchange Commission (“SEC”) on March 11, 2014, solely to correct Exhibits 31.1, 31.2, 32.1 and 32.2. The remainder of the Annual Report on Form 10-K is included for convenience only and, except for corresponding updates to the cover page, Part IV and signature page, reflects the content of the Company's original Annual Report on Form 10-K for the year ended December 28, 2013, filed with the SEC on March 11, 2014. This Amendment No. 1 has not been updated to reflect any events occurring after the filing of the Company’s original Annual Report on Form 10-K for the year ended December 28, 2013, filed with the SEC on March 11, 2014.

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Forward-Looking Statements

This Annual Report on Form 10-K contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. Any statements about our expectations, beliefs, plans, objectives, assumptions or future events or performance are not historical facts and may be forward-looking. We use words or phrases such as “anticipates,” “believes,” “could,” “estimates,” “expects,” “intends,” “plans,” “predicts,” “projects,” “may,” “will,” “should,” “continue,” “ongoing,” “future,” “potential” and phrases to identify forward-looking statements. Examples of forward-looking statements include, but are not limited to, statements about: our strategies and beliefs regarding the markets we serve or may serve; growth opportunities and growth in markets we may serve; acceptance of programmable logic devices and displacement of other general purpose logic solutions; our plans to introduce new FPGA families in high-growth market niches where we believe that we have sustainable and differentiated positions; the costs of making and developing various general purpose logic products; our intention to continually introduce new products and enhancements and reduce manufacturing costs; the majority of our revenue being through our sell-through distributors; the impact of our global tax structure and expectations regarding taxes and tax adjustments; our expectations that a significant portion of our revenue will continue to be dependent on the Consumer, Communications, Industrial, Scientific and Medical, and Computing end markets; the Asia Pacific market being the primary source of our revenue; our plans to sell our auction rate securities; the costs and benefits and timing of completion of our restructuring plans; the impact of new accounting pronouncements; our expectations regarding customer preferences and product use; our future product development and marketing plans; our ability to maintain or develop successful foundry relationships to produce new products; our expectations regarding seasonal trends; our expectations regarding defenses to claims against our intellectual property; our making significant future investments in research and development; our beliefs concerning the adequacy of our liquidity and facilities, and our ability to meet our operating and capital requirements and obligations.

Forward-looking statements involve estimates, assumptions, risks and uncertainties that could cause actual results to differ materially from those expressed in the forward-looking statements. The key factors that could cause our actual results to differ materially from the forward-looking statements include global economic conditions and uncertainty, the concentration of our sales in the consumer and communications equipment end market, particularly as it relates to the concentration of our sales in the Asia Pacific region, market acceptance and demand for our new products, any disruption of our distribution channels, unexpected charges, delays or results relating to our restructuring plans, the effect of the downturn in the economy on capital markets and credit markets, the impact of competitive products and pricing, unanticipated taxation requirements, or positions of the U.S. Internal Revenue Service, unexpected impacts of recent accounting guidance and the other risks that are described herein and that are otherwise described from time to time in our filings with the Securities and Exchange Commission, including, but not limited to, the items discussed in “Risk Factors” in Item 1A of Part I of this Report. You should not unduly rely on forward-looking statements because our actual results could differ materially from those expressed in any forward-looking statements made by us. In addition, any forward-looking statement applies only as of the date on which it is made. We do not plan to, and undertake no obligation to, update any forward-looking statements to reflect events or circumstances that occur after the date on which such statements are made or to reflect the occurrence of unanticipated events.

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PART I

Item 1. Business.

Lattice Semiconductor Corporation ("Lattice," the "Company," "we," "us," or "our") designs, develops and markets programmable logic products and related software. We also provide design services, customer training, field engineering and technical support.

Lattice was incorporated in Oregon in 1983 and reincorporated in Delaware in 1985. Our headquarters facility is located at 5555 N.E. Moore Court, Hillsboro, Oregon 97124, and our website is www.latticesemi.com. Information contained or referenced on our website is not incorporated by reference into, and does not form a part of, this Annual Report on Form 10-K. Our common stock trades on the NASDAQ Global Select Market under the symbol LSCC.

We report based on a 52 or 53-week fiscal year ending on the Saturday closest to December 31. Our fiscal 2013, 2012, 2011, and 2010 were 52-week years that ended December 28, 2013, December 29, 2012, December 31, 2011, and January 1, 2011, respectively. Our fiscal 2014 will be a 53-week year and will end on January 3, 2015. All references to quarterly or yearly financial results are references to the results for the relevant fiscal period.

Programmable Logic Market Background

Three types of digital integrated circuits are used in most electronic systems: microprocessors, memory and logic.

- Microprocessors are used for control and computing tasks.
- Memory is used to store programming instructions and data.
- Logic is employed to manage the interchange and manipulation of digital signals within a system.

Logic circuits are found in a wide range of today's digital electronic equipment, including communications, computing, consumer, industrial, scientific, medical, automotive, and military systems. The general purpose logic market for semiconductor solutions can be subdivided into three primary categories:

- Application-specific integrated circuits ("ASICs") are custom devices for a single user, which generally entail significant design risks, non-recurring expenses and longer development cycles. ASICs have historically been perceived as having advantages of lower unit costs, higher performance and lower power when compared to PLDs.
- Application-specific standard products ("ASSPs") are standardized logic devices marketed to multiple users, with limited flexibility to customize an end system. ASSPs have historically been perceived as having similar advantages as ASICs (ie: cost, performance and power) relative to programmable logic devices with the additional benefit of being readily available as an off-the-shelf standard product, thereby avoiding the risk and non-recurring engineering associated with ASICs.
- Programmable logic devices, including those offered by Lattice, are standard semiconductor products, purchased by systems manufacturers in a "blank" state that can be custom-configured into a virtually unlimited number of specific logic functions.

Industry sources have estimated that the general purpose logic and application-specific semiconductor product categories combined to account for approximately 37% of the estimated $318 billion worldwide semiconductor market in 2013. Based on those sources, we believe that the programmable logic market was approximately $4.5 billion in 2013.

Programmable logic devices have key competitive advantages over ASICs and ASSPs that make them suitable for certain types of applications, including:

- Faster time to market and increased design flexibility. These advantages are enabled by development software allowing users to implement and revise their designs quickly. ASICs and ASSPs, on the other hand, require significant development time and offer limited, if any, flexibility to make design changes.
- Programmable logic devices are standard components, meaning that the same device can be sold to many different users for a variety of applications, while ASICs and ASSPs are customized for an individual use or specific application.

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Programmable Logic Market

There are two main subcategories of programmable logic devices: field programmable gate arrays (“FPGAs”) and conventional programmable logic devices (“PLDs”), each representing distinctly different silicon architectural approaches.

- FPGAs are traditionally characterized by a narrow-input logic cell and use a distributed interconnect scheme. FPGAs may also contain dedicated blocks of fixed circuits such as memory, high-speed input/output interfaces or processors.
- PLDs are traditionally characterized by a regular building block structure of wide-input logic cells, called macrocells, and use a centralized logic interconnect scheme.

Although FPGAs and PLDs are typically suited for use in distinct types of logic applications, with PLDs being well-suited for 'control-oriented' applications and FPGAs being well-suited for 'data-path' applications, we believe that a substantial portion of programmable logic customers have needs for, and could utilize both FPGAs and PLDs. In addition, mixed signal programmable logic devices that combine digital and analog features are growing in popularity. We offer solutions utilizing all of these silicon architectures to serve multiple markets in a wide variety of applications. Throughout this Annual Report we generally use the term FPGAs when referring to both our FPGAs and our PLDs.

End Markets for Our FPGAs

An overview of the end market applications for our products is shown in the following table:

End Markets	Sub-Market	Applications	Tethered	Mobile
Communications	Wireless	Base Station	X	
		Wireless Backhaul	X	
		Heterogeneous Networks	X	
	Wireline	Routers and Switches	X	
		Data Centers	X	
		Carrier Class Wifi	X	
		Wired access aggregation	X	
Consumer		Smartphones		X
		Wearables		X
		Tablets & E-Readers		X
		Digital SLR Cameras		X
		GPS navigation units		X
		High Definition Televisions	X	
		Laptops and PCs	X	X
		Gaming	X	X
Industrial, Scientific and Medical (ISM)	Industrial	Factory Automation	X	X
		Motor and Process Controls	X	X
		Video Surveillance & Security	X	X
	Scientific	Human-Machine Interface	X	X
		Test and Measurement	X	X
	Medical	Diagnostic Imaging	X	X
		Hand-held Medical Devices	X	X
	Automotive	Driver Assistance Systems	X	X
		Driver Information Systems	X	X
Computing		Servers and Micro Servers	X	
		Data Centers	X	
		Storage networks	X	

	Security	X

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Lattice Strategy and Advantage

We believe that the number of devices that are always-on, always-connected and connected-to-everything (the "Internet of Things") which could benefit from our products will continue to expand, providing growth opportunities in many of the markets we serve today. Our strategy is to lead the middle-to-low-end of the FPGA market where high density, system-level integration, and the most advanced process technology are less necessary and to displace ASICs and ASSPs in applications where low cost, low power, small form factor, and rapid time to market are critical to the success of our customers.

The following table summarizes the key characteristics of our FPGAs relative to ASICs and ASSPs:

	Lattice FPGAs	ASICs/ASSPs
Time to Market	Fast	Slow
Development Cost (non-recurring engineering)	Lower	Higher
Customizable by User	Yes	No
Hardware Reprogrammability	Yes	No
Process Technology	Advanced	Often Lagging

We believe that the rapid pace of change and increasing complexity of products and connectivity places a premium on the programmable flexibility, rapid time to market, and relatively lower development costs and risks associated with our products when compared to ASICs and ASSPs.

Where time to market is critical to our customers, the reprogrammability of an FPGA solution allows designers to more quickly and simply add features, easily correct mistakes and/or fill gaps in other functions. Additionally, our focus on the development of customizable design solutions for our FPGAs ("IP Cores") provides customers with reliable, pre-tested, reusable functions that can be quickly adopted, allowing our customers to direct their time and energy on the unique aspects of their product. This can provide FPGAs a distinct time to market advantage over competing solutions.

Another advantage for certain of our FPGA solutions are their relatively advanced process technologies, often one or more generations ahead of competing ASICs, microcontrollers and ASSPs. This generational advantage from a lithography standpoint allows lower end FPGAs to compete directly on power and cost while offering a distinct advantage in form factor. We expect the fixed cost of ASIC and ASSP development to significantly increase on more advanced technology nodes, allowing FPGAs to better address high volume applications and gain market share from ASIC and ASSP suppliers.

The following table summarizes certain key characteristics of our FPGAs relative to higher density FPGAs offered by other FPGA companies:

	Lattice FPGAs	Higher Density FPGAs
Size	Smaller	Larger
Unit Cost	Lower	Higher
Power Consumption	Lower	Higher

Higher density FPGAs are large, expensive and consume greater power. Integrating multiple functions including high-end processors on a single device often requires expensive and advanced process technologies that lead to higher development and manufacturing costs. We have chosen not to compete at the high-end of this traditional FPGA market. Rather, we focus on providing more flexible solutions in the middle and low-end of the market by leveraging established process nodes to create multiple generations of cost effective devices on mature process technologies. By

leveraging established, lower cost ttd align="left" valign="bottom" width="71%" style="border-bottom: #ffffff solid;">

	Three Months Ended March 31,	
	2008	2007
	(Unaudited)	(Unaudited)
Revenues		
	$ 12,413,430	$ 5,179,116
Cost of Goods Sold	2,860,428	1,126,695
Gross Profit	9,553,002	4,052,421
Operating Expenses		
Selling, general and administrative	3,956,795	2,043,776
Depreciation and amortization	76,348	83,355
Research and development	669,833	15,210

Total operating expenses		
	4,702,976	
	2,142,341	
Other Income (Expense)		
Other income		
	63,048	
	-	
Interest expense		
	(1,147)	
	(16,494)	
Total other income (expense)		
	61,901	
	(16,494)	
Net Income Before Provision for Income Tax		
	4,911,927	
	1,893,586	
Provision for Income Taxes		
Current		
	1,047,016	
	344,265	
Net Income		
$	3,864,911	
$	1,549,321	

Basic Earnings Per Share	
$	0.28
$	0.13
Basic Weighted Average Shares Outstanding	
	13,732,269
	12,036,524
Diluted Earnings Per Share	
$	0.26
$	0.12
Diluted Weighted Average Shares Outstanding	
	14,888,310
	12,498,303
The Components of Other Comprehensive Income	
Net Income	
$	3,864,911
$	1,549,321
Foreign currency translation adjustment	
	1,620,516
	258,766
Comprehensive Income	
$	**5,485,427**
$	**1,808,087**

See accompanying summary of accounting policies and notes to the condensed consolidated financial statements.

China Sky One Medical, Inc. and Subsidiaries
Consolidated Statements of Cash Flows

	Three Months Ended March 31, 2008 (Unaudited)	2007 (Unaudited)
Cash flows from operating activities		
Net Income	$ 3,864,911	$ 1,549,321
Adjustments to reconcile net cash provided by operating activities		
Depreciation and amortization	140,009	87,579
Share-based compensation expense	10,117	10,117
Net change in assets and liabilities		
Accounts receivables and other receivables	1,859,639	(1,369,449)
Inventories	(408,079)	(509,889)
Prepaid expenses	5,526	14,564
Accounts payable and accrued liabilities	(456,219)	765,133
Advances by customers	-	(67,541)
Wages payable	94,178	38,920
Welfare payable	(8,337)	13,147
Taxes payable	102,786	29,775
Deferred revenue	(6,952)	-
Net cash provided by operating activities	5,197,579	561,677
Cash flows from investing activities		
Purchases of fixed assets	(42,782)	(693,667)
Land deposit	(710,656)	-
Purchase of subsidiary-Heilongjiang Haina Pharmaceutical, Inc.	(427,838)	-
Cash of subsidiary upon acquisition	82,715	-
Purchase of intangible assets	(7,139)	(66,239)
Net cash used in investing activities	(1,105,700)	(759,906)
Cash flows from financing activities		
Sale of common stock for cash	25,000,000	-
Board and syndication costs	(1,512,037)	-
Proceeds from warrants conversion	739,588	-
Proceeds from short-term loan	-	5,124
Net cash provided by (used in) financing activities	24,227,551	5,124
Effect of exchange rate	727,694	316,552
Net increase in cash	29,047,124	123,447
Cash and cash equivalents at beginning of year	9,190,870	6,586,800
Cash and cash equivalents at end of period	$ 38,237,994	$ 6,710,247
Supplemental disclosure of cash flow information		
Interest paid	$ 1,157	$ 5,940
Taxes paid	$ 944,230	$ -
Share-based compensation expense	$ 10,117	$ 10,117

See accompanying summary of accounting policies and notes to the condensed consolidated financial statements.

China Sky One Medical, Inc. and Subsidiaries
Notes to the Condensed Consolidated Financial Statements
As of March 31, 2008

1. Description of Business

The accompanying unaudited consolidated financial statements of China Sky One Medical, Inc., a Nevada corporation, and subsidiaries have been prepared in accordance with generally accepted accounting principles ("GAAP") for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by U.S. GAAP for complete financial statements. The financial statements for the periods ended March 31, 2008 and 2007 are unaudited and include all adjustments necessary to a fair statement of the results of operations for the periods then ended. All such adjustments are of a normal recurring nature. The results of the company's operations for any interim period are not necessarily indicative of the results of the company's operations for a full fiscal year. For further information, refer to the financial statements and footnotes thereto included in the company's annual report on Form 10-K for the year ended December 31, 2007 as filed with the Securities and Exchange Commission ("SEC") on March 31, 2008.

China Sky One Medical, Inc. ("China Sky One" or the “Company”), a Nevada corporation, was formed on February 7, 1986, and formerly known as Comet Technologies, Inc. (“Comet”). On July 26, 2006, the change in the name of the reporting company from "Comet Technologies, Inc." to "China Sky One Medical, Inc.," became effective.

American California Pharmaceutical Group, Inc. (“ACPG”), our non operating United States holding company subsidiary, was incorporated on December 16, 2003, in the State of California, under the name “QQ Group, Inc.” It changed its name to “American California Pharmaceutical Group, Inc.” in anticipation of the Stock Exchange Agreement with China Sky One (then known as “Comet Technologies, Inc.”) and TDR, described herein. On December 8, 2005, ACPG completed a stock exchange transaction with TDR a PRC based operating company and TDR’s subsidiaries (the “TDR Acquisition”), each of which were fully operating companies in the PRC. Under the terms of the agreement, ACPG exchanged 100% of its issued and outstanding common stock for 100% of the capital stock of TDR and its subsidiaries, described below.

Thereafter, on May 11, 2006, ACPG entered into a Stock Exchange Agreement (the “Exchange Agreement”) with the shareholders of China Sky One. The terms of the Exchange Agreement were consummated and the acquisition was completed on May 30, 2006. As a result of the transaction, the Company issued a total of 10,193,377 shares of its common voting stock to the stockholders of ACPG, in exchange for 100% of the capital stock of ACPG resulting in ACPG becoming our wholly-owned subsidiary. The transaction is treated as a reverse merger for accounting purposes.

TDR, formerly known as “Harbin City Tian Di Ren Medical Co.,” was originally formed in 1994 and maintained its principal executive office in Harbin City of Heilongjiang Province, in the PRC. TDR was reorganized and incorporated as a limited liability company on December 29, 2000, under the “Corporation Laws and Regulations” of the PRC. At the time of the TDR Acquisition by ACPG in December of 2005, TDR had two wholly-owned subsidiaries, Harbin First Bio-Engineering Company Limited and Kangxi Medical Care Product Factory, until July, 2006, when the two were merged, with Harbin First Bio-Engineering Company Limited (“First”) as the surviving subsidiary of TDR. The principal activities of TDR and First are the research, manufacture and sale of over-the-counter non-prescription health care products. TDR commenced its business in the sale of branded nutritional supplements and over-the-counter pharmaceutical products in the Heilongjiang Province. TDR has subsequently evolved into an integrated manufacturer, marketer, and distributor of external use natural Chinese medicine products sold primarily to and through China’s various domestic pharmaceutical chain stores.

China Sky One is a holding company whose principal operations are through its subsidiaries; it has no revenues separate from its subsidiaries, and has nominal expenses related to its status as a public reporting company and to its ownership interest in ACPG, TDR and TDR’s subsidiaries in the PRC.

On April 3, 2008, TDR completed an acquisition pursuant to an Equity Transfer Agreement dated February 22, 2008, between TDR and Heilongjiang Tianlong Pharmaceutical, Inc., a corporation with a multitude of SFDA approved medicines and new medicine applications, organized under the laws of the PRC ("Heilongjiang"), which is in the business of manufacturing external-use pharmaceuticals. Our TDR subsidiary previously acquired the Beijing sales office of Heilongjiang in mid 2006. Pursuant to the Equity Transfer Agreement, TDR acquired 100% of the issued and outstanding capital stock of Heilongjiang from Heilongjiang's sole stockholder Wu Jiechen, a resident of China, in consideration for an aggregate purchase price of approximately $8,300,000, consisting of (i) approximately $8,000,000 in cash, and (ii) approximately $300,000 of shares of common stock (24,809 shares, $.001 par value per share) of the Registrant.

On April 18, 2008, China Sky One through its subsidiary Harbin TDR consummated a share acquisition pursuant to an Equity Transfer Agreement with the shareholders of Heilongjiang Haina Pharmaceutical Inc., a recently formed corporation organized under the laws of the PRC ("Haina") licensed as a wholesaler of TCD, bio-medicines, bio-products, medicinal devices, antibiotics and chemical medicines. Haina Pharmaceutical does not have an established sales network and was acquired for its primary asset, a Good Supply Practice (GSP) license (License No. A-HLJ03-010) issued by the Heilongjian office of the SFDA. The SFDA recently started issuing such licenses to resellers of medicines that maintain certain quality controls. The GSP license was issued as of December 21, 2006 and will expire on January 29, 2012 and will enable the Company to expand its sales of medicinal products without having to go through a lengthy license application process.

Pursuant to the Equity Transfer Agreement, TDR acquired 100% of the issued and outstanding capital stock of Haina from its three stockholders in consideration for payment of 3,000,000 RMB (approximately $428,571). TDR has been overseeing the operations of Haina Pharmaceutical since January of 2008 as part of its due diligence prior to closing of this acquisition.

2. Basis of Preparation of Financial Statements

The accompanying financial statements differ from the financial statements used for statutory purposes in PRC in that they reflect certain adjustments, recorded on the entities' books, which are appropriate to present the financial position, results of operations and cash flows in accordance with US GAAP. Such differences are immaterial.

Principles of Consolidation – The consolidated financial statements include the accounts of the Company and its subsidiaries, ACPG, TDR, First, and Haina. All inter-company transactions and balances were eliminated.

These financial statements are stated in U.S. Dollars and have been prepared in accordance with accounting principles generally accepted in the United States of America. This basis of accounting differs from that used under applicable accounting requirements in the PRC. No material adjustment was required. Certain amounts in prior years have been reclassified to conform to current year's classification.

3. Summary of Significant Accounting Policies

Use of estimates – The preparation of these financial statements in conformity with accounting principles generally accepted in the United States of America, requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the dates of the financial statements, and the reported amounts of revenues and expenses during the reported periods.

Significant estimates included values and lives assigned to acquired intangible assets, reserves for customer returns and allowances, uncollectible accounts receivable, valuation of equity issuances such as shares of the Company's common stock and stock options to purchase shares of the Company's common stock, and slow moving and/or obsolete/damaged inventory. Actual results may differ from these estimates.

Earnings per share - Basic net earnings per common share is computed by dividing net earnings applicable to common shareholders by the weighted-average number of common shares outstanding during the period. Diluted net earnings per common share is determined using the weighted-average number of common shares outstanding during the period, adjusted for the dilutive effect of common stock equivalents, consisting of shares that might be issued upon exercise of common stock options and warrants.

Cash and cash equivalents – The Company considers all highly liquid debt instruments purchased with maturity period of three months or less to be cash equivalents. The carrying amounts reported in the accompanying consolidated balance sheet for cash and cash equivalents approximate their fair value.

Accounts receivable – Accounts receivable are stated at net realizable value, net of an allowance for doubtful accounts. Provision of allowance is made for estimated bad debts based on a periodic analysis of individual customer balances including an evaluation of days of sales outstanding, payment history, recent payment trends, and perceived credit worthiness. At March 31, 2008 and December 31, 2007, the Company had no allowance for doubtful accounts.

Inventories – Inventories include finished goods, raw materials, freight-in, packing materials, labor, and overhead costs accounted for using the weighted average method. Provisions are made for slow moving, obsolete and/or damaged inventory based on a periodic analysis of individual inventory items including an evaluation of historical usage and/or movement, age, expiration date, and general conditions. There was no provision provided at March 31, 2008.

Property and equipment – Property and equipment are stated at the historical cost less accumulated depreciation. Depreciation on property, plant, and equipment is provided using the straight-line method over the estimated useful lives of the assets. An estimated residual value of 5% of cost, or valuation, was made for each items for both financial and income tax reporting purposes. The estimated lengths of useful lives are as follows:

Buildings	30 years
Land use rights	50 years
Furniture & Equipments	5 to 7 years
Motor vehicles	5 to 15 years
Machineries	7 to 14 years

Expenditures for renewals and betterments were capitalized while repairs and maintenance costs were normally charged to the statement of operations in the year in which they were incurred. In situations where it can be clearly demonstrated that the expenditure has resulted in an increase in the future economic benefits expected to obtain from the use of the asset, the expenditure is capitalized as an additional cost of the asset. Upon sale or disposal of an asset, the historical cost and related accumulated depreciation or amortization of such asset were removed from their respective accounts, and any gain or loss was recorded in the Consolidated Statements of Operations.

Property and equipment are evaluated for impairment in value annually or whenever an event or change in circumstances indicates that the carrying values may not be recoverable. If such an event or change in circumstances occurs and potential impairment is indicated because the carrying values exceed the estimated future undiscounted cash flows of the asset, the Company would measure the impairment loss as the amount by which the carrying value of the asset exceeds its fair vale.

Construction-in-progress – Properties currently under development are accounted for as construction-in-progress. Construction-in-progress is recorded at acquisition cost, including land rights cost, development expenditure, professional fees, and the interest expenses for the purpose of financing the project capitalized during the course of construction.

Upon completion and readiness for use of the project, the cost of construction-in-progress is to be transferred to the facility. In the case of construction-in-progress, management takes into consideration the estimated cost to complete the project when making the lower of cost or market calculation.

Intangible assets – Intangible assets consists of patents, distribution rights and customer lists. Patent costs are being amortized over a total life of ten years. Distribution rights and customer lists are being amortized over 10 years.

Intangible assets are accounted for in accordance with Statement of Financial Accounting Standards No. 142, *Goodwill and Other Intangible Assets* (“SFAS 142”). Intangible assets with finite useful lives are amortized while intangible assets with indefinite useful lives are not amortized. As prescribed by SFAS 142, goodwill and intangible assets are tested periodically for impairment. The Company adopted SFAS No. 144, "Accounting for the Impairment or Disposal of Long- Lived Assets," effective January 1, 2002. Accordingly, the Company reviews its long-lived assets, including property and equipment and finite-lived intangible assets for impairment whenever events or changes in circumstances indicate that the carrying amount of the assets may not be fully recoverable. To determine recoverability of its long-lived assets, the Company evaluates the probability that future undiscounted net cash flows

will be less than the carrying amount of the assets. Impairment costs, if any, are measured by comparing the carrying amount of the related assets to their fair value. There were no impairments as of March 31, 2008.

Foreign Currency - The Company's principal country of operations is in The People's Republic of China. The financial position and results of operations of the Company are recorded in RMB as the functional currency. The results of operations denominated in foreign currency are translated at the average rate of exchange during the reporting period.

Assets and liabilities denominated in foreign currencies at the balance sheet date are translated at the market rate of exchange ruling at that date. The registered equity capital denominated in the functional currency is translated at the historical rate of exchange at the time of capital contribution. All translation adjustments resulting from the translation of the financial statements into the reporting currency ("US Dollars") are dealt with as a separate component within shareholders' equity.

Revenue recognition– Revenue is recognized in accordance with Staff Accounting Bulletin No. 104, Revenue Recognition, which states that revenue should be recognized when the following criteria are met: (1) persuasive evidence of an arrangement exists; (2) the product has been shipped and the customer takes ownership and assumes the risk of loss; (3) the selling price is fixed or determinable; and (4) collection of the resulting receivable is reasonably assured. The Company believes that these criteria are satisfied upon shipment from its facilities. Revenue is reduced by provisions for estimated returns and allowances as well as specific known claims, if any, which are based on historical averages that have not varied significantly for the periods presented.

The Company occasionally applies to various government agencies for research grants. Revenue from such research grants is recognized when earned. In situations where TDR receives payment in advance for the performance of research and development services, such amounts are deferred and recognized as revenue as the related services are performed.

Interest income is recognized when earned, taking into account the average principal amounts outstanding and the interest rates applicable.

Deferred revenues - The Company recognizes revenues as earned. Amounts billed in advance of the period in which goods are delivered are recorded as a liability under "Deferred revenue." As of March 31, 2008 the Company has $18,540 in deferred revenue.

Shipping and Handling costs - Shipping and handling costs are included in selling, general and administrative expenses and totaled $103,616 for the three months ended March 31, 2008.

Research and development—Research and development expenses include the costs associated with the Company's internal research and development as well as research and development conducted by third parties. These costs primarily consist of salaries, clinical trials, outside consultants, and materials. All research and development costs discussed above are expensed as incurred.

Third-party expenses were reimbursed under non-refundable research and development contracts, and are recorded as a reduction to research and development expense in the statement of operations.7

The Company recognizes in-process research and development in accordance with FASB Interpretation No. 4, *Applicability of FASB Statement No. 2 to Business Combinations Accounted for by the Purchase Method* and the AICPA Technical Practice Aid, Assets Acquired in a Business Combination to be used in Research and Development Activities: A Focus on Software, Electronic Devices, and Pharmaceutical Industries. Assets to be used in research and development activities, specifically, compounds that have yet to receive new drug approval and would have no alternative use, should approval not be given, are immediately charged to expense when acquired.

For the three months ended March 31, 2008, the Company incurred $ 669,833 in research and development expenditures, and $15,210 for the three months ended March 31, 2007.

Advertising—The Company expensed advertising and promotion expenses as they are incurred. The total advertising expenses incurred for the three months ended March 31, 2008 and 2007 was $369,995 and $478,776, respectively.

Taxation – The Company uses the asset and liability method of accounting for deferred income taxes. The Company's provision for income taxes includes income taxes currently payable and those deferred because of temporary differences between the financial statement and tax bases of assets and liabilities. The Company records liabilities for income tax contingencies based on our best estimate of the underlying exposures.

The Company periodically estimates its probable tax obligations using historical experience in tax jurisdictions and informed judgments. There are inherent uncertainties related to the interpretation of tax regulations in the jurisdictions in which the Company transacts business. The judgments and estimates made at a point in time may change based on the outcome of tax audits, as well as changes to, or further interpretations of, regulations. The Company adjusts income tax expense in the period in which these events occur.

Provision for the PRC's enterprise income tax is calculated at the prevailing rate based on the estimated assessable profits less available tax relief for losses brought forward.

Provision for the PRC enterprise income tax is calculated at the prevailing rate based on the estimated assessable profits less available tax relief for losses brought forward**.** The Company does not accrue taxes on unremitted earnings from foreign operations as it is the Company's intention to invest these earnings in the foreign operations indefinitely**.**

Enterprise income tax

Under the Provisional Regulations of The People's Republic of China Concerning Income Tax on Enterprises promulgated by the PRC, income tax is payable by enterprises at a rate of 25% of their taxable income. Preferential tax treatment may, however, be granted pursuant to any law or regulations from time to time promulgated by the State Council.

According to "Enterprise Income Tax and Certain Preferential Policies Notice" published by the Ministry of Finance and the National Tax Affairs Bureau, if the enterprise is authorized by the State Council as a special entity, the enterprise income tax rate is reduced to 15%. The income tax rate for TDR is 15% based on State Council approval.

Value added tax

The Provisional Regulations of The People's Republic of China Concerning Value Added Tax promulgated by the State Council came into effect on January 1, 1994. Under these regulations and the Implementing Rules of the Provisional Regulations of the PRC Concerning Value Added Tax, value added tax is imposed on goods sold in, or imported into, the PRC and on processing, repair and replacement services provided within the PRC.

Value added tax payable in the PRC is charged on an aggregated basis at a rate of 13% or 17% (depending on the type of goods involved) on the full price collected for the goods sold or, in the case of taxable services provided, at a rate of 17% on the charges for the taxable services provided, but excluding, in respect of both goods and services, any amount paid in respect of value added tax included in the price or charges, and less any deductible value added tax already paid by the taxpayer on purchases of goods and services in the same financial year.

According to "Agriculture Product Value Added Tax Rate Adjustment and Certain Items' Value Added Tax Waiver" published by the Ministry of Finance and the National Tax Affairs Bureau, the value added tax for agriculture related products is to be taxed at 13%. Furthermore, traditional Chinese medicine and medicinal plant are by definition agriculture related products.

Comprehensive Income – Comprehensive income consists of net income and other gains and losses affecting shareholders' equity that, under generally accepted accounting principles are excluded from net income. For the Company, such items consist entirely of foreign currency translation gains and losses

Related companies – A related company is a company in which the director has beneficial interests in and in which the Company has significant influence.

Retirement benefit costs – According to the PRC regulations on pension plans, the Company contributes to a defined contribution retirement plan organized by municipal government in the province in which the Company was registered and all qualified employees are eligible to participate in the plan.

Contributions to the pension or retirement plan are calculated at 23.5% of the employees' salaries above a fixed threshold amount. The employees contribute between 2% to 8% to the pension plan, and the Company contributes the balance contribution of from 21.5% to 15.5%. The Company has no other material obligation for the payment of retirement benefits beyond the annual contributions under this plan.

Fair value of financial instruments – The carrying amounts of certain financial instruments, including cash, accounts receivable, commercial notes receivable, other receivables, accounts payable, commercial notes payable, accrued expenses, and other payables approximate their fair values as at March 31, 2008 because of the relatively short-term maturity of these instruments.

Recent accounting pronouncements:

- In February 2007, the FASB issued Statement No. 159 “The Fair Value Option for Financial Assets and Financial Liabilities” (SFAS 159). This statement permits companies to choose to measure many financial assets and liabilities at fair value. Unrealized gains and losses on items for which the fair value option has been elected are reported in earnings. SFAS 159 is effective for fiscal years beginning after November 15, 2007. The Company is currently assessing the impact of SFAS 159 on its consolidated financial statements.
- In December 2007, the FASB issued SFAS No. 141 (revised 2007), “Business Combinations” (“SFAS 141(R)”). SFAS 141(R) will change the accounting for business combinations. Under SFAS No. 141(R), an acquiring entity will be required to recognize all the assets acquired and liabilities assumed in a transaction at the acquisition-date fair value with limited exceptions. SFAS No. 141(R) will change the accounting treatment and disclosure for certain specific items in a business combination. SFAS No. 141(R) applies prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2008. SFAS 141(R) will impact the Company in the event of any future acquisition.
- In December 2007, the FASB issued SFAS No. 160, “Non-controlling Interests in Consolidated Financial Statements—an amendment of Accounting Research Bulletin No. 51” (“SFAS 160”). SFAS 160 establishes new accounting and reporting standards for the non-controlling interest in a subsidiary and for the deconsolidation of a subsidiary. SFAS No. 160 is effective for fiscal years beginning on or after December 15, 2008. The Company does not believe that SFAS 160 will have a material impact on its consolidated financial statements.
- In March 2008, the FASB issued Statement No. 161, *Disclosures about Derivative Instruments and Hedging Activities* ("SFAS 161"). This Statement will require enhanced disclosures about derivative instruments and hedging activities to enable investors to better understand their effects on an entity's financial position, financial performance, and cash flows. It is effective for financial statements issued for fiscal years and interim periods beginning after November 15, 2008, with early application encouraged. We are assessing the impact of the adoption of this Statement.

4. Concentrations of Business and Credit risk

The Company maintains certain bank accounts in the PRC which are not protected by FDIC insurance or other insurance. As of March 31, 2008 the Company held $2,601,706 of cash balances within the United States of which $2,301,706 was in excess of FDIC insurance limits. At March 31, 2008, the Company had approximately $35,636,288, in China bank deposits, which may not be insured. The Company has not experienced any losses in such accounts through March 31, 2008 and December 31, 2007.

Geographic Concentration; Fluctuations in Regional Economic Conditions. Nearly all of the Company’s sales are concentrated in China. Accordingly, the Company is susceptible to fluctuations in its business caused by adverse economic conditions in this country. Difficult economic conditions in other geographic areas into which the Company may expand may also adversely affect its business, operations and finances.

The Company provides credit in the normal course of business. Substantially all customers are located in The People's Republic of China. The Company performs ongoing credit evaluations of its customers and maintains allowances for doubtful accounts based on factors surrounding the credit risk of specific customers, historical trends, and other information.

Substantially all of the Company's fixed assets and operations are located in the Peoples Republic of China.

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The Company is self-insured for all risks and carries no liability or property insurance coverage of any kind.

Substantially all of the Company's profits are generated from operations in mainland China.

Major Customers

As of March 31, 2008 Xinteyao Ltd. accounted for approximately 14 % of the Company’s sales. During the years ended December 31, 2007, Ningbo Yuehua Trading Co. accounted for approximately 14 % of the Company’s sales. Beijing Huali Jiuzhou Medical Ltd. accounted for 11% of all accounts receivable as of March 31, 2008.

Major Suppliers

Purchases from Heilongjiang Kangda Medicine Co. accounted for approximately 45% of the Company’s purchases for the three months ended March 31, 2008. There were no major single suppliers for materials during the three months ended March 31, 2007.

Payments of dividends may be subject to some restrictions due to the Company’s operating subsidiaries all being located in the PRC.

5. Earnings per Share

We have applied SFAS No. 128, “Earnings Per Share” in its calculation and presentation of earnings per share - “basic” and “diluted”. Basic earnings per share are computed by dividing income available to common shareholders (the numerator) by the weighted average number of common shares (the denominator) for the period. The computation of diluted earnings per share is similar to basic earnings per share, except that the denominator is increased to include the number of additional common shares that would have been outstanding if the potentially dilutive common shares had been issued.

Stock warrants and options to purchase 1,452,665 shares of common stock, all were exercisable during the three months ended March 31, 2008, and Stock warrants and options to purchase 1,868,510 shares of common stock, all were exercisable during the three months ended March 31, 2007, were included in the computation of diluted earnings per share because the average market price of our common stock were less than the option exercise prices during these periods.

The dilutive potential common shares on warrants and options is calculated in accordance with the treasury stock method, which assumes that proceeds from the exercise of all warrants and options are used to repurchase common stock at market value. The amount of shares remaining after the proceeds are exhausted represent s the potential dilutive effect of the securities.

The following table sets forth our computation of basic and diluted net income (loss) per share:

	Three Months ended March 31,	
	2008	**2007**
Numerator:		
Net income (loss) used in calculation of basic earnings (loss) per share	$ **3,864,911**	$ **1,549,321**
Net income (loss) used in calculation of diluted earnings (loss) per share	$ **3,864,911**	$ **1,549,321**
Denominator:		
Weighted-average common shares outstanding used in calculation of basic earnings (loss) per share	13,732,269	12,036,524
Effect of dilutive securities:		
Stock options and equivalents	**1,156,041**	**461,779**
Weighted-average common shares used in calculation of diluted earnings (loss) per share	**14,888,310**	**12,498,303**
Net income (loss) per share:		
Basic	$ 0.28	$ 0.13
Diluted	$ 0.26	$ 0.12

6. Equity and Share-based Compensation

Effective January 1, 2006, we adopted the fair value recognition provisions of SFAS No. 123R, Share-Based Payment ("SFAS No. 123R"), for options granted to employees and directors, using the modified prospective transition method, and therefore have not restated results from prior periods. Compensation cost for all stock-based compensation awards granted after March 31, 2005 is based on the grant date fair value estimated in accordance with the provisions of SFAS No. 123R. Under the fair value recognition provisions of SFAS No. 123R, we recognize stock-based compensation net of an estimated forfeiture rate and only recognize compensation cost for those shares expected to vest on a straight-line prorated basis over the requisite service period of the award. In March 2005, the SEC issued Staff Accounting Bulletin ("SAB") No. 107, Share-Based Payment ("SAB No. 107"), regarding the SEC's guidance on SFAS No. 123R and the valuation of share-based payments for public companies. We have applied the provisions of SAB No. 107 in the adoption of SFAS No. 123R. Under SFAS 123R, the company remeasures the intrinsic value of the options at the end of each reporting period until the options are exercised, cancelled or expire unexercised.

In July 2006, the Company's stockholders approved the 2006 Stock Incentive Plan (the "2006 Plan"). The 2006 Plan, provides for the grant of stock options, restricted stock awards, and performance shares to qualified employees, officers, directors, consultants and other service providers. The 2006 Plan originally authorized the Company to grant options and/or rights to purchase up to an aggregate of 1,500,000 shares of common stock. As of March 31, 2008, non-qualified options to purchase a total of 113,500 shares have been granted under the 2006 Stock Incentive Plan. All options were granted in October 2006. All options have an exercise price of $3.65 per share, the weighted fair market value on the date of grant was $4.25 per share. Of these 113,500 options a total of 60,500 were granted to employees and a total of 53,000 were granted to consultants. These options were valued under the following Black-Scholes assumptions: no dividends; risk-free interest rate of 4%; a contractual life of 5 years and volatility of 39%. An additional 50,000 shares registered under the 2006 Plan were issued outright to employees of the company. All 113,500 options vest over various periods for the various options granted to employees and consultants. There

were no options granted in the three months ended March 31, 2008. As of March 31, 2008, these options have a remaining life of approximately 4 years, and remain outstanding and continue to be remeasured at the intrinsic value over their remaining vesting period ranging from 6 months to 2 years. Compensation expense in any given period is calculated as the difference between total earned compensation at the end of the period, less total earned compensation at the beginning of the period. Compensation earned is calculated on a straight line basis over the requisite service period for any give option award. The effect of adoption of the new standard for the three months ended March 31, 2008 and 2007 related to stock options to employees were additional non-cash expenses of $10,117 and $10,117, respectively.

Options or stock awards issued to non-employees and consultants are recorded at their fair value as determined in accordance with SFAS No. 123R and EITF No. 96-18, "Accounting for Equity Instruments That Are Issued to Other Than Employees for Acquiring, or in Conjunction with Selling, Goods or Services", and recognized over the related vesting or service period. In connection with closing of the Stock Exchange Agreement, the Company agreed to grant warrants to advisors for the services they already performed for the reverse merger in July 2006, entitling them to purchase up to 500,000 shares on or before July 31, 2009, at a price of US$2.00 per share and options to purchase up to 50,000 shares on or before December 20, 2008 at a price of US$3.00 per share. The fair value of these warrants and options were determined to be $772,275 and deducted as expenses using the Black-Scholes option-pricing model with the following weighted assumptions: no dividends; risk-free interest rate of 4%; the contractual life of 2.5-3.5 years and volatility of 39%. The Company based its estimate of expected volatility on the historical, expected or implied volatility of similar entities whose share or option prices are publicly available.

One January 3, 2007, the holder of 50,000 warrants dated March 11, 1999, granted prior to the May 30, 2006 company reorganization, stock exchange exercised the warrants by electing to use cashless conversion provision of the warrants and acquired 5,160 shares of the Company common stock (after giving effect to the 8-to 1 reverse stock split effected after the warrant was issued). These warrants are not included in the schedule below.

At various times during the three months ended March 31, 2008 warrant holder exercised their warrants, at various exercise prices, for total proceeds of $739,588.

7. **Securities Purchase Agreement and Related Transaction**

On January 31, 2008 China Sky One entered into a Securities Purchase Agreement (the "Securities Purchase Agreement") with certain accredited investors, for the purchase and sale of units consisting of: (i) one (1) share of the Company's common stock, $.001 par value per share ("Common stock"); and (ii) 750,000 Class A Warrants exercisable at $12.50 per share, and expiring on July 31, 2011 (the "Class A Warrants"), for a purchase price of $10.00 per Unit (the "January 2008 Offering"), and gross offering proceeds of $25,000,000.

Holders of the 2,500,000 shares of common stock sold in our January 2008 Offering have certain put rights and rights to receive additional shares from the Company if we sell low priced securities or from certain key shareholders in the event that certain thresholds are not met, in addition to registration rights. Specifically, these investors have:

- The right to receive additional shares of common stock from China Sky One in the event that we sell shares (or convertible securities or warrants convertible into or exercisable for common stock) prior to January 31, 2009 at per share price (or exercise or conversion price) of less than $10.00, in such amount so as to reduce the average price paid by such shareholder to the price per share being paid by the new investors,

- The right to receive up to 3,000,000 shares deposited into escrow by our principal shareholder, in the event that the Company fails to attain Earnings Per Share, as adjusted of at least (i) $1.05 per share for fiscal year ended December 31, 2007 based on fully diluted shares outstanding before the January 2008 offering (an aggregate of 13,907,696), and/or (ii) $1.75 per share for fiscal year ending December 31, 2008 based on fully diluted shares outstanding after the January 2008 Offering (an aggregate of 16,907,696 shares). While the Company has satisfied the criterion of (i) above for 2007, no assurance can be made that we will satisfy our earnings goal next year.

The Class A Warrants represent the right to purchase an aggregate of 750,000 shares of common stock, at an exercise price of $12.50 per share. Additional information relating to these Class A Warrants is provided in the following “Note 8” to this Quarterly Report on Form 10-Q.

8. Detail of the outstanding warrants and options

	Shares Underlying Warrants	**Weighted average Exercise Price Warrants**	**Shares underlying Options**	**Weighted average Exercise Price Options**
Outstanding as of January 1, 2006	25,000	$ 1.50	-	
Granted	1,650,000	2.58	163,500	$ 3.45
Exercised	-	-	-	-
Expired or cancelled	-	-	-	-
Outstanding as of December 31, 2006	**1,675,000**	**2.57**	**163,500**	**$ 3.45**
Granted	-	-	-	-
Exercised	-	-	-	-
Expired or cancelled	(161,667)	3.19	-	-
Outstanding as of December 31, 2007	**1,513,333**	**$ 2.48**	**163,500**	**$ 3.45**
Granted	750,000	12.50	-	-
Exercised	(224,168)	3.30	-	-
Expired or cancelled	-	-	-	-
Outstanding as of March 31, 2008	**2,039,165**	**$ 6.08**	**163,500**	**$ 3.45**

The following table summarizes information about stock warrants outstanding and exercisable as of March 31, 2008.

Exercise Price	Outstanding March 31, 2008	Weighted Average Remaining Life in Years	Number exercisable
$ 2.00	1,000,000	1.33	1,000,000
$ 3.00	10,000	.53	10,000
$ 3.50	279,165	.53	279,165
$ 12.50	750,000	3.0	-
	2,039,165		**1,289,165**

Out of the 2,039,165 outstanding warrants, 1,289,165 shares were exercisable as of March 31, 2008. The remaining Class A Warrants represent the right to purchase an aggregate of 750,000 shares of Common Stock of the Company granted with the Securities Purchase Agreement, at an exercise price of $12.50 per share, and have the following additional characteristics:

The Class A Warrants issued in our January 2008 Offering described in Note 7 above, represent the right to purchase an aggregate of 750,000 shares of common stock, at an exercise price of $12.50 per share, and have the following additional characteristics:

- The Class A Warrants are exercisable beginning on the six-month anniversary of the closing of the January 2008 Offering and will expire July 31, 2011.

- Commencing on one-year anniversary of the Closing Date, in the event the Warrant Shares may not be freely sold by the holders of the Class A Warrants due to the Company's failure to satisfy its registration requirements, and an exemption for such sale is not otherwise available to the Warrant-holders under Rule 144, the Class A Warrants will be exercisable on a cashless basis.

- The Exercise Price and number of Warrant Shares will be subject to adjustment for standard dilutive events, including the issuance of Common stock, or securities convertible into or exercisable for shares of Common stock, at a price per share, or conversion or exercise price per share less than the Class A Warrant exercise price of $12.50 per share.

- At anytime following the date a Registration Statement covering the Warrant Shares is declared effective, we will have the ability to call the Class A Warrants at a price of $0.01 per Class A Warrant, upon thirty (30) days prior written notice to the holders of the Class A Warrants, provided (i) the closing price of the Common stock exceeded $18.75 for each of the ten (10) consecutive trading days immediately preceding the date that the call notice is given by the Company, and (ii) the Company has attained an Adjusted EPS of at least $1.75 per share for the fiscal year ending December 31, 2008, as set forth in our audited financial statements of the Company.

- If, among other things, we fail to cause a Registration Statement covering the Warrant Shares to be declared effective prior to the applicable dates set forth in the Registration Rights Agreement, the expiration date of the Class A Warrants shall be extended one day for each day beyond the Effectiveness Deadlines.

- If a Warrant-holder exercises its Put Right under the Put Agreement (defined in Item 1.01 above), such Warrant-holder's right to exercise the Class A Warrants shall be suspended, pending the satisfaction of our obligations to pay the Warrant-holder the applicable Repurchase Price. Upon receipt of the Repurchase Price in full by the Warrant-holder, the Warrant-holder's right to exercise the Class A Warrants shall automatically and

permanently terminate and expire, and the Class A Warrants shall be immediately cancelled on the books of the Company.

The following table summarizes information about stock options outstanding as of March 31, 2008.

Exercise Price	Outstanding March 31, 2008	Weighted Average Remaining Life in Years	Exercisable Options	Unvested Options
$ 3.00	50,000	.72	50,000	-
$ 3.65	113,500	3.75	54,150	59,350
	163,500		104,150	59,350

9. Inventories

The Company values its inventories at the lower of cost and market method. Inventories are accounted for using the first-in, first-out method. Inventories in the balance sheet include packing materials, raw materials, supplemental materials, work-in-process, and finished products.

As of March 31, 2008 and December 31, 2007, inventories consist of the following:

	March 31, 2008	December 31, 2007
Raw Material	$ 249,730	$ 252,318
Supplemental Material	81,307	32,296
Work-in-Process	154,039	57,337
Finished Products	309,654	29,721
Total Inventory	**$ 794,730**	**$ 371,672**

10. Property and Equipment

All of TDR and its subsidiaries' buildings and fixed assets are located in the PRC and the land is used pursuant to a land use right granted by the PRC for 50 years commencing in 2004. As of March 31, 2008 and December 31, 2007, Property and Equipment consist of the following:

	March 31, 2008	December 31, 2007
Buildings	$ 2,976,316	2,861,011
Machinery and equipment	1,633,220	1,568,958
Land use rights	583,162	563,469
Automobiles	374,010	318,779
Furniture and Equipments	104,288	96,501
Construction in progress	2,199,155	2,113,957
Total Property and Equipment	7,870,151	7,522,675
Less: Accumulated Depreciation	(759,965)	(661,243)
Property and Equipment, Net	**$ 7,110,186**	**$ 6,861,432**

For the three months ended March 31, 2008 and 2007, depreciation expenses totaled $70,560 and $31,131 respectively.

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11. Intangible Assets

As of the three months ended March 31, 2008 and December 31, 2007, the Company's unamortized intangible assets consist of:

	March 31, 2008	December 31, 2007
Patents	$ 1,948,374	$ 1,599,814
Distribution rights and customer lists	336,730	333,200
Total Intangible Assets, net	**$ 2,285,104**	**$ 1,933,014**

Amortization expense for the three months ended March 31, 2008 and March 31, 2007 was $69,449 and $ 56,448 respectively.

Patents are amortized over the life of the patent of ten years and the distribution rights and customer lists are amortized over ten years.

12. Taxes Payable

As of March 31, 2008, taxes payable consists of the following:

	March 31, 2008	December 31, 2007
Value Added Tax, net	$ 619,343	$ 612,602
Enterprise Income Tax	1,069,451	940,819
City Tax	17,378	4,789
Other Taxes and additions	26,963	8,978
Total Taxes Payable	**$ 1,733,135**	**$ 1,567,188**

13. Land Purchase Agreement

During the second quarter in 2007 TDR entered into an agreement with the Development and Construction Administration Committee of Harbin Song Bei New Development district to purchase the land use rights for 50 years for development of a new biotech engineering project. Terms of the agreement called for a deposit of 30% of the total land price within 15 days after signing the agreement, 40% payment 7 days prior to the start of construction and the balance of 30% 7 days after getting the formal land use right.

The project consists of two phases:

(1) Construction of main workshop, R&D center and office using land area of 30,000 square meters. Construction started in May 2007 and is projected to be completed by June 2008.
(2) Construction of Second workshop and show room using land area of 20,000 square meters. Construction is expected to start in September 2008 to be completed by December 2009.

TDR has committed to the Development and Construction Administration Committee of the Harbin Song Bei New Development District that the minimum investment per square meter will be $394.

As of March 31, 2008 and December 31, 2007, the Company has deposits totaling $9,036,409 and $8,003,205 respectively, related to the acquisition of these land use rights.

14. Commitments and Contingencies

The formulation, manufacturing, processing, packaging, labeling, advertising, distribution and sale of external use Chinese medicine such as those sold by the Company are subject to regulations by one or more federal agencies. The principal federal agencies include the State Food and Drug Administration of the Government of the Peoples Republic of China, the Food and Drug Administration (the “FDA”), Heilongjiang Provincial Food and Drug Administration of the People's Republic of China (PFDA), National Biology Products Inspection Institute (NBPI) and the National Food and Drug Administration (NFDA) of the People's Republic of China and, to a lesser extent, the Consumer Product Safety Commission. These activities are also regulated by various governmental agencies for the countries, states and localities in which the Company’s products are sold.

Although management believes that the Company is in material compliance with the statutes, laws, rules and regulations of every jurisdiction in which it operates, no assurance can be given that the Company’s compliance with the applicable statutes, laws, rules and regulations will not be challenged by governing authorities or private parties, or that such challenges will not lead to material adverse effects on the Company’s financial position, results of operations, or cash flows.

The Company, like any other distributor or manufacturer of products that are designed to be ingested, exposes the Company to the inherent risk of product liability claims in the events of possible injuries caused by the use of its products. The Company does not have liability insurance with respect to product liability claims; the insurance environment of China is neither sufficient nor mature. Inadequate insurance or lack of contractual indemnification from parties supplying raw materials or marketing its products, and product liabilities related to defective products could have material adverse effects on the Company.

The Company is not involved in any legal matters arising in the normal course of business. While incapable of estimation, in the opinion of the management, the individual regulatory and legal matters in which it might involve in the future are not expected to have a material adverse effect on the Company’s financial position, results of operations, or cash flows.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

FORWARD LOOKING STATEMENTS

The following discussion should be read in conjunction with the information contained in the consolidated financial statements of the Company and the notes thereto appearing elsewhere herein and in the risk factors and "Forward Looking Statements" summary set forth in the forepart of this Annual Report as well as the "Risk Factors" section above and are afforded the safe harbor provisions of Section 27A of the Securities Act and Section 21E of the Securities Exchange Act of 1934, as amended. Readers should carefully review the risk factors disclosed in this Annual Report and other documents filed by us with the SEC.

DISCUSSION

We primarily generate revenues, through our China based indirect subsidiaries described below, in the development, manufacture, marketing and sale of over-the-counter, branded nutritional supplements and over-the-counter plant and herb based pharmaceutical and medicinal products. Our principal products are external use Traditional Chinese Herbal Remedies/ Medicines commonly referred to in the industry as "TCM." We have evolved into an integrated manufacturer, marketer and distributor of external use Chinese medicine products sold primarily in China and through Chinese domestic pharmaceutical chains and have been expanding our worldwide sales effort as well. We sell both our own manufactured products, as well as medicinal and pharmaceutical products manufactured by others in China.

The Company achieved continuing growth on the sale of both our own product line and a contract service line of manufacturer's products which we sell through our distribution channel. For the three months ended March 31, 2008, total revenue was $12,413,430, a 140% increased over the same period in 2007, and the first three months of 2008 net income was $3,864,911, or $0.26 per share on a diluted basis compared to net income of $1,549,321, or $0.13 per share on a diluted basis in the same period in 2007.

All of our business is conducted through our wholly-owned subsidiary, ACPG which, in turn, wholly owns Harbin Tian Di Ren Medical Science and Technology Company (referred to herein as "TDR") a company organized in the PRC and TDR's subsidiaries, described above and below.

TDR, formerly known as "Harbin City Tian Di Ren Medical Co.," was originally formed in 1994 and maintained its principal executive office in Harbin City of Heilongjiang Province, in the PRC. TDR was reorganized and incorporated as a limited liability company on December 29, 2000, under the "Corporation Laws and Regulations" of the PRC. At the time of the TDR Acquisition by ACPG in December of 2005, TDR had two wholly-owned subsidiaries, Harbin First Bio-Engineering Company Limited and Kangxi Medical Care Product Factory, until July, 2006, when the two were merged, with Harbin First Bio-Engineering Company Limited ("First" or "Harbin Bio Engineering") as the surviving subsidiary of TDR.

We have also recently organized Harbin Tian Qing Biotech Application Company as a wholly-owned PRC subsidiary of TDR, to conduct research and development in the areas of tissue and stem cell banks, which is described in more detail below.

Recent Developments

On April 3, 2008, TDR completed an acquisition pursuant to an Equity Transfer Agreement dated February 22, 2008, between TDR and Heilongjiang Tianlong Pharmaceutical, Inc., ("Heilongjiang"), a corporation with a multitude of SFDA approved medicines and new medicine applications, organized under the laws of the PRC which is in the business of manufacturing external-use pharmaceuticals. Our TDR subsidiary previously acquired the Beijing sales office of Heilongjiang in mid 2006. Pursuant to the Equity Transfer Agreement, TDR acquired 100% of the issued and

outstanding capital stock of Heilongjiang from Heilongjiang's sole stockholder Wu Jiechen, a resident of China, in consideration for an aggregate purchase price of approximately $8,300,000, consisting of (i) approximately $8,000,000 in cash, and (ii) approximately $300,000 of shares of common stock (24,809 shares, $.001 par value per share) of the Registrant. The seller had no material relationship with the Registrant or any of its affiliates, or any director or officer of the registrant, or any associate of any such director or officer.

On April 18, 2008, TDR consummated a share acquisition pursuant to an Equity Transfer Agreement with the shareholders of Heilongjiang Haina Pharmaceutical Inc., a recently formed corporation organized under the laws of the PRC ("Haina") licensed as a wholesaler of TCD, bio-medicines, bio-products, medicinal devices, antibiotics and chemical medicines. Haina Pharmaceutical does not have an established sales network and was acquired for its primary asset, a Good Supply Practice (GSP) license (License No. A-HLJ03-010) issued by the Heilongjian office of the SFDA. The SFDA recently started issuing such licenses to resellers of medicines that maintain certain quality controls. The GSP license was issued as of December 21, 2006 and will expire on January 29, 2012 and will enable the Company to expand its sales of medicinal products without having to go through a lengthy license application process.

Pursuant to the Equity Transfer Agreement, TDR acquired 100% of the issued and outstanding capital stock of Haina Pharmaceutical from its three stockholders in consideration for payment of 3,000,000 RMB (approximately $428,571). TDR has been overseeing the operations of Haina Pharmaceutical since January of 2008 as part of its due diligence prior to closing of this acquisition.

Summary of Our Research and Development Activities

We currently conduct all of our research and development ("R&D") activities, either internally or through collaborative arrangements with universities and research institutions in the PRC. We have our own research, development and laboratory facilities located at TRD's principal headquarters in the city of Harbin, Heilongjiang Province.

Additionally, we have established several long-term partnerships with well-known universities and enterprises in the PRC. We have built a gene medicine laboratory through a collaborative effort with Harbin Medical University; established a cell laboratory with North East Agricultural University; and founded a monoclonal antibody laboratory with Jilin University. The foregoing are more fully described in our annual report.

In collaboration with Harbin Medical University, we have completed a laboratory experimental study pertaining to Endothelin-1, which is required prior to clinical trials, and we are currently applying for approval to enter clinical experiments. This medicine has been recognized by the PRC as the "Top Category in New Medicine." In order to qualify as the "Top Category in New Medicine," a company must have intellectual property rights, high technology involvement, strong innovation, and the medicine must be the first of its kind to be introduced to the PRC. We hold the intellectual property rights pertaining to this technology, and we have obtained an invention patent to this intellectual property in the PRC. Under our partnership arrangements with other universities and research institutions, we will generally hold the intellectual property rights to any developed technology.

At present, our ongoing research is divided into five general areas: (1) the development of an enzyme linked immune technique to prepare extraneous diagnostic kits (see table below); (2) the development of an enzyme linked gold colloid technique to prepare extraneous rapid diagnostic test strip; (3) the development of a gene recombination technique to prepare gene drug; (4) the development of a biology protein chip for various tumor diagnostic applications; and (5) the development of a cord blood stem cell bank, as more fully described in other reports of the Company.

We currently have eight biological products under development: HIV detection kit; a uterus cancer diagnostic kit; a breast cancer diagnostic kit; a liver cancer diagnostic kit; a rectum cancer diagnostic kit; a gastric cancer diagnostic kit; a gene recombination drug; and a multi-tumor marker protein chip detection kit. We are also working to establish additional sales networks and cell banks covering domestic and international markets.

Testing Kits and Other Products in Production

We also have three products: AMI Diagnostic Kit, Human Urinary Albumin Elisa Kit and Early Pregnancy Diagnostic Kit that have passed the final stages of national inspection in 2006 or 2007. These diagnostic kits are being sold through drug stores, hospitals, examination stations and independent sales agents throughout the PRC. We also plan to market these products in Vietnam, Indonesia, Philippines and eventually in Africa. We expect our sales in this product category to increase in mid 2008.

Our AMI Diagnostic Kit, which entered markets in 2007, is used for early diagnosis of Myocardial Infarction (MI), also known as heart disease. All the test kits require users to place a blood or urine sample on the marker and a positive (+) or negative (-) reaction signal will result, showing if a user should consult his or her doctor for further testing. According to the China Medical Newspaper, Several million people die from MI every year. MI often occurs to people who are, but not limited to, smokers, over-weight and diabetic. There are approximately 8 million new MI patients in China every year. Recent medical studies have shown that heart failure or heart attacks are increasing among younger people in China. This is a result from a more modern life style, the fast pace of city life and increased pressure from work or school. The use of AMI Diagnostic Kits will help in early detection that can help in reducing these statistics.

We are continuing our marketing efforts with respect to these testing kits which we anticipate will result in continued increased sales of these products in 2008.

Significant Accounting Estimates and Policies

The discussion and analysis of our financial condition and results of operations is based upon our financial statements which have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets and liabilities. On an on-going basis, we evaluate our estimates including the allowance for doubtful accounts, the salability and recoverability of our products, income taxes and contingencies. We base our estimates on historical experience and on other assumptions that we believes to be reasonable under the circumstances, the results of which form our basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

Property and equipment are evaluated for impairment whenever indicators of impairment exist. Accounting standards require that if an impairment indicator is present, we must assess whether the carrying amount of the asset is unrecoverable by estimating the sum of the future cash flows expected to result from the asset, undiscounted and without interest charges. If the recoverable amount is less than the carrying amount, an impairment charge must be recognized based on the fair value of the asset.

As part of the process of preparing our consolidated financial statements, we are required to estimate our income taxes. This process involves estimating our current tax exposure together with assessing temporary differences resulting from differing treatment of items for tax and accounting purposes. These differences result in deferred tax assets and liabilities. We must then assess the likelihood that our deferred tax assets will be recovered from future taxable income, and, to the extent we believe that recovery is not likely, we must establish a valuation allowance. To the extent that we establish a valuation allowance or increase this allowance in a period, we must include a tax provision or reduce our tax benefit in the statements of operations. We use our judgment to determine our provision or benefit for income taxes, deferred tax assets and liabilities and any valuation allowance recorded against our net deferred tax assets. We believe, based on a number of factors including historical operating losses, which we will not realize the future benefits of a significant portion of our net deferred tax assets and we have accordingly provided a full valuation allowance against our deferred tax assets. However, various factors may cause those assumptions to change in the near term.

We cannot predict what future laws and regulations might be passed that could have a material effect on our results of operations. We assess the impact of significant changes in laws and regulations on a regular basis and update the assumptions and estimates used to prepare our financial statements when we deem it necessary.

We have determined the significant principles by considering accounting policies that involve the most complex or subjective decisions or assessments. Our most significant accounting policies are those related to intangible assets and research and development.

Intangible assets - Intangible assets consist of patents, distribution rights and customer lists. Patent costs are being amortized over the remaining term of the patent. Distribution rights and customer lists are being amortized over 10 years.

Intangible assets are accounted for in accordance with Statement of Financial Accounting Standards No. 142, *Goodwill and Other Intangible Assets* ("SFAS 142"). Intangible assets with finite useful lives are amortized while intangible assets with indefinite useful lives are not amortized. As prescribed by SFAS 142, goodwill and intangible assets are tested periodically for impairment. The Company adopted SFAS No. 144, "Accounting for the Impairment or Disposal of Long- Lived Assets," effective January 1, 2002. Accordingly, the Company reviews its long-lived assets, including property and equipment and finite-lived intangible assets for impairment whenever events or changes in circumstances indicate that the carrying amount of the assets may not be fully recoverable. To determine recoverability of its long-lived assets, the Company evaluates the probability that future undiscounted net cash flows will be less than the carrying amount of the assets. Impairment costs, if any, are measured by comparing the carrying amount of the related assets to their fair value.

Research and development—Research and development expenses include the costs associated with the Company's internal research and development as well as research and development conducted by third parties. These costs primarily consist of salaries, clinical trials, outside consultants, and materials. All research and development costs discussed above are expensed as incurred.

Third-party expenses were reimbursed under non-refundable research and development contracts, and are recorded as a reduction to research and development expense in the statement of operations.

The Company recognizes in-process research and development in accordance with FASB Interpretation No. 4, *Applicability of FASB Statement No. 2 to Business Combinations Accounted for by the Purchase Method* and the AICPA Technical Practice Aid, Assets Acquired in a Business Combination to be used in Research and Development Activities: A Focus on Software, Electronic Devices, and Pharmaceutical Industries. Assets to be used in research and development activities, specifically, compounds that have yet to receive new drug approval and would have no alternative use, should approval not be given, are immediately charged to expense when acquired.

For the three months ended March 31, 2008, the Company incurred $669,833 in research and development expenditures, and $15,210 for year 2007.

RESULTS OF OPERATIONS

Three months ended March 31, 2008 as compared to Three months ended March 31, 2007

Our principal business operations are conducted through our wholly owned subsidiary, TDR, and TDR's subsidiaries. The results of operations of TDR have been included in the below financial statements since the acquisition date.

		2008	March 31 Variance		2007
REVENUES					
Product Sales (net of sales allowance)	$	9,467,414	174%	$	3,457,558
Contract Sales		2,946,016	71%		1,721,558
Total revenues	$	12,413,430	140%		5,179,116
COST OF GOOD SOLD					
Cost of good sold		2,860,428	154%		1,126,695
Gross Profit	**$**	**9,553,002**	**136%**	**$**	**4,052,421**

Total sales increased by 140% in the three months ended March 31, 2008 compared to 2007. The $7.2 million increase in sales is attributable to strong performances from our sales distribution channel.

Product sales increased by 174% in the three months ended March 31, 2008, to $9,467,414 from $ 3,457,558 in 2007. This growth in sales is attributable to volume and continuing efforts to develop our distribution channels by hiring direct territory managers and sales agents to assure that our products and their associated benefits are seen by those making or influencing the purchasing decisions. A new subsidiary, Haina Medical (Haina) contributed $1.8 million to the product sales. TDR's product sales in the three months ended March 31, 2008, which accounted for 81% of the total product sales for the same period, increased 114% over 2007.

Contract and Other Revenue

The following table summarizes the period over period changes in our contract and other revenues:

		March 31 2008	Change		2007
Contract and other revenue	$	2,946,016	71%	$	1,721,558

Contract and other revenue was $2,946,016 in the three months ended March 31, 2008, or a significant increase of $ 1,224,458 over sales of $1,721,558 in 2007. In 2008, contract and other revenue increased primarily due to net product distribution service revenue from sales of other manufactured brands through our distribution channel, which constitutes approximately 31% of total sales in 2008.

Sales by Product Line

A break-down of our sales by product line for the three months ended March 31 2008 and 2007 is as follows:

	Three Months Ended March 31,						
	2008			2007			
Product category	*Quantity (Kilogram)*	*Sales USD*	*% of Sales*	*Quantity (Kilogram)*	*Sales USD*	*% of Sales*	*Period-on-period Quantity Variance*
Spray	723,142	1,863,371	15%	534,729	1,344,730	26%	188,413
Plaster	126,623	362,478	3%	101,099	268,550	5%	25,524
Ointment	1,163,937	1,487,146	12%	417,680	615,322	12%	746,257
Cleaning Liquid	353,423	493,293	4%	245,810	295,041	6%	107,613
Lose weight Series	261,100	2,026,719	16%	9,127	79,964	2%	251,973
Antihypertension	136,969	1,408,792	11%	93,187	884,647	17%	43,782
Bio-chemical Products	278,320	1,825,615	15%	19,622	3,890	0%	258,698
Contract sales	1,525,670	2,946,016	24%	952,481	1,686,972	32%	573,189
Total	**4,569,184**	**12,413,430**	**100%**	**2,373,735**	**5,179,116**	**100%**	

There were various changes in the break-down of sales among our product lines over the three months ended March 31, 2008 as we are now operating an additional subsidiary and are in the process of developing new products and new markets. As shown in the table above, sales volume for all product increased as compared to the three months ended March 31, 2007. To maintain our competitiveness in the PRC market, unit selling prices were reduced, however, as overall selling prices in the Chinese market decreased. Decrease of unit selling prices was also due to negotiation with certain significant customers.

Cost of Goods Sold and Product Gross Margin

		March 31 2008	December Variance		2007
Total sales	$	12,413,430	140%	$	5,179,116
Cost of goods sold	$	2,860,428	154%	$	1,126,695
Product gross margin		**77%**			**78%**

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Our product's gross margin was 77% for first quarter 2008, compared to 78% of first quarter 2007. Although the unit selling price for the three months ended 2008 decreased compared to the comparable period in 2007, cost of sales decreased at a similar rate as more product sales were from self- production. As a result, the product gross margin decreased only 1% compared to the three months ended 2007.

Selling, General and Administrative Expenses.

The following table summarizes the period over period changes in our selling, general and administrative expenses over the last two years:

		2008	March 31 Variance		2007
Operating Expenses					
R&D Expenses	$	669,833	4304%	$	15,210
General, administrative and selling expenses		3,956,795	94%		2,043,776
Depreciation and amortization		76,348	(8)%		83,355
Total operating expenses		4,702,976	120%		2,142,341
Other (Income) Expenses					
Other income		(63,048)			-
Interest expense		1,147			16,494
Total other (income) expenses	$	(61,901)		$	16,494

Gross sales increased approximately $7.2 million in the three months ended March 31, 2008 and corresponding, selling, general and administrative expenses for the three months ended March 31, 2008 increased by $2.0 million over 2007. Selling expenses increased 90% due to the increase of sales. General and administrative expenses increased 359% compare to 2007.

Research and development expenses were $669,833 in the three months ended March 31, 2008 compared to $15,210 for 2007. We anticipate R&D expenses will increase as we conduct additional clinical trials and seek out additional patents and claims for our products.

2008 Outlook

We expect slaes in 2008 to increase by 62% to approximately $80 million with increase in all categories of our product sales. Sales are expected to increase $0.77 million in Spray products, $0.27 million in Plaster products, $5.32 million in Ointment products, $0.62 million in Cleaning Liquid products, $5.60 million in Lose Weight Series, $0.77 million in Antihypertension products, $8.07 million in Bio-chemical products. Contract sales are expected to decrease $5 million due to the acquisition of Heilongjiang Tianlong Pharmaceutical, Inc. while sales from Heilongjiang Tianlong Pharmaceuticalwill increase $14.40 million. We expect our cost of sales will increase $6.26 million, gross profit will increase $24.52 million, and gross margin will be at 78.5%.

LIQUIDITY AND CAPITAL RESOURCES

The following table summarizes our cash, cash equivalents and marketable securities, our working capital, and our cash flow activity as of the end of, and for each of, three months period for the last two years:

		2008		2007
As of March 31:				
Cash, cash equivalents and marketable securities	$	38,237,994	$	6,710,247
Working capital	$	43,563,886		9,001,591
Three Months Ended March 31:				
Cash provided by (used in):				
Operating activities	$	5,197,579	$	561,677
Investing activities	$	(1,105,700)	$	(759,906)
Financing activities	$	24,227,551	$	5,124

As of March 31, 2008, cash and cash equivalents were $38,237,994, an increase of 470% over March 31, 2007. The increase of $31.5 million in 2007 was primarily due to: an increase net income of $2.3 million and the issuance of 2,500,000 shares of common stock for $24.2 million.

The Company’s current ratio at March 31, 2008 was 9.77, and quick ratio was 9.60. Its primary sources of funds include cash balances, cash flow from operations, and sales of equity. Management endeavors to ensure that funds are available to take advantage of new investment opportunities and that funds are sufficient to meet future liquidity and capital needs. Management considers current working capital and borrowing capabilities adequate to cover the Company's current operating and capital requirements.

There was no restrictive bank deposit pledged as of March 31, 2008. Therefore, the Company did not have to maintain any minimum balance in the relevant deposit account as security.

Cash flows provided by operating activities were $5.2 million for the three months ended March 31, 2008 compared to cash provided by operating activities of $562,000 for the comparable 2007 period. The increase in cash provided by operating activities of $4.6 million was attributable primarily to the greater sales compared to three months ended March 31, 2007.

Working capital at March 31, 2008 was $43.6 million, compared to $9.0 million at March 31, 2007. Significant factors that resulted in an increase in 2008 working capital were: a $31.5 million increase in cash, cash equivalents, and a $5.0 million increase in accounts receivable primarily due to increased sales of $7.2 million in three months ended March 31, 2008.

These increases were partially offset by: a $ 1.1 million increase in income taxes payable primarily due to higher profitability; a $916,000 increase in accounts payable, and other accrued liabilities including increases in accruals in wages.

Inventories increased only marginally as of March 31, 2008, from 2007. The Company has a small inventory on hand primarily due to the enhanced productivity of newly purchased equipment and machinery, and the popularity of Company products in the market.

QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

As of March 31, 2008, the Company had no material derivative instruments. The Company may enter into derivative financial instrument transactions in order to mitigate its interest rate risk on a related financial instrument in the future.

Our balance sheet includes amount of assets and liabilities whose fair values are subject to market risk. Market risk is the risk of loss arising from adverse changes in market prices or interest rates. Generally, the Company's borrowing is short to medium term in nature and therefore approximates fair value. The Company currently has interest rate risk as it relates to its fixed maturity mortgage participation interest. The Company seeks to limit the impact of interest rate changes on earnings and cash flows and to lower its overall borrowing costs by closely monitoring its interest rate debt.

The Company has certain equity risks as it relates to its marketable equity securities, and foreign currency risks as it relates to investments denominated in foreign currencies. The Company and its subsidiaries are mainly located in China, and there were no significant changes in exchange rates, during the reported periods. However, unforeseen developments may cause a significant change in exchange rates. The Company is subject to commodity price risks arising from price of construction materials.

The Company is subject to market and channel risks. Over 90% of the Company's sales are made in the PRC, where the Company primarily sells its products through drug chain stores. Because of this, the Company is dependent to a large degree upon the success of that distribution channel as well as the success of specific retailers in the distribution channel. Many of the drug stores are individual stores or very small chains, and only a few are large chain drug stores. The Company relies on these distribution channels to purchase, market, and sell its products. The Company's success is dependent, to a large degree, on the growth and success of the drug stores, which may be outside its control. There can be no assurance that the drug store distribution channels will be able to grow or prosper as it faces price and service pressure from other channels, including the mass market. There can be no assurance that retailers in the drug store distribution channel, in the aggregate, will respond or continue to respond to the Company's marketing commitment in these channels.

The Company is highly dependent upon the public perception and quality of its products, consumers' perception of the safety and quality of its products, as well as similar products distributed by other companies. Thus, the mere publication of reports asserting that such products may be harmful could have a material adverse effect on the Company, regardless of whether these reports are scientifically supported. Adverse publicity may have a material adverse effect on the Company's business, financial condition, and results of operations. There can be no assurance of future favorable scientific results and media attention, or of the absence of unfavorable or inconsistent findings.

Currency Exchange Fluctuations

All of Company's revenues and majority of the expenses in 2007 were denominated primarily in Renminbi ("RMB"), the currency of China, and was converted into US dollars at the exchange rate of 7.006 RMB to 1 U.S. Dollar. In the third quarter of 2005, the Renminbi began to rise against the US dollar. There could be no assurance that RMB-to-U.S. dollar exchange rates will remain stable. A devaluation of RMB relative to the U.S. dollar would adversely affect our business, financial condition and results of operations. We do not engage in currency hedging.

Off-Balance Sheet Arrangements

We do not have any off-balance sheet arrangements that are currently material or reasonably likely to be material to our financial position or results of operations.

Item 3. Quantitative and Qualitative Disclosures About Market Risk.

As of March 31, 2008, the Company had no material derivative instruments. The Company may enter into derivative financial instrument transactions in order to mitigate its interest rate risk on a related financial instrument in the future.

Our balance sheet includes amount of assets and liabilities whose fair values are subject to market risk. Market risk is the risk of loss arising from adverse changes in market prices or interest rates. Generally, the Company's borrowing is short to medium term in nature and therefore approximates fair value. The Company currently has interest rate risk as it relates to its fixed maturity mortgage participation interest. The Company seeks to limit the impact of interest rate changes on earnings and cash flows and to lower its overall borrowing costs by closely monitoring its interest rate debt.

The Company has certain equity risks as it relates to its marketable equity securities, and foreign currency risks as it relates to investments denominated in foreign currencies. The Company and its subsidiaries are mainly located in China, and there were no significant changes in exchange rates, during the reported periods. However, unforeseen developments may cause a significant change in exchange rates. The Company is subject to commodity price risks arising from price of construction materials.

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The Company is highly dependent upon the public perception and quality of its products, consumers' perception of the safety and quality of its products, as well as similar products distributed by other companies. Thus, the mere publication of reports asserting that such products may be harmful could have a material adverse effect on the Company, regardless of whether these reports are scientifically supported. Adverse publicity may have a material adverse effect on the Company's business, financial condition, and results of operations. There can be no assurance of future favorable scientific results and media attention, or of the absence of unfavorable or inconsistent findings.

Currency Exchange Fluctuations

All of Company's revenues and majority of the expenses in the first quarter ended March 31, 2008 of fiscal 2008 were denominated primarily in Renminbi ("RMB"), the currency of China, and was converted into US dollars at the exchange rate of 7.006 RMB to 1 U.S. Dollar. In the third quarter of 2005, the Renminbi began to rise against the US dollar. There could be no assurance that RMB-to-U.S. dollar exchange rates will remain stable. A devaluation of RMB relative to the U.S. dollar would adversely affect our business, financial condition and results of operations. We do not engage in currency hedging.

Off-Balance Sheet Arrangements

We do not have any off-balance sheet arrangements that are currently material or reasonably likely to be material to our financial position or results of operations.

Item 4. Controls and Procedures.

The Company's management, with the participation of the Company's Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of the Company's disclosure controls and procedures as of March 31, 2008. Based on that evaluation, the Company's Chief Executive Officer and Chief Financial Officer concluded that the

Company's disclosure controls and procedures were effective as of March 31, 2008.

Changes in Internal Control Over Financial Reporting

There was no change in our internal control over financial reporting that occurred during our first quarter ended March 31, 2008 of fiscal 2008, that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting. The Company regularly reviews its internal controls and plans on updating and expanding the same as an accelerated filer.

PART II - OTHER INFORMATION

Item 1. Legal Proceedings.

We are not a party to any pending legal proceedings.

Item 1A. Risk Factors.

In the three month period ended March 31, 2008, and subsequent period through the date hereof, there were no material changes to our risk factors previously disclosed in Item 1. to Part 1 of our Annual Report on Form 10-KSB for the year ended December 31, 2007.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds.

In the three-month period ended March 31, 2008, and subsequent period through the date hereof, other than as previously reported (as such term is defined in Rule 12b-2) we did not engage in any unregistered sales of equity securities other then as a result of the exercise of various options and warrants.

In all, an aggregate of 243,018 shares were issued upon exercise of warrants or options held by 12 persons between January 1, 2008 and March 31, 2008, at exercise prices varying between $3.00 and $3.50. An additional 110,000 shares were issued upon exercise of warrants or options and employee options held by 5 persons since March 31, 2008 and the date hereof.

Management believes that these transactions were exempt from the registration requirements of the Securities Act of 1933, as amended (the “Securities Act”) since, among other exemptions, pursuant to Regulation D and Section 4(2) of the Securities Act, since sales were made on an unsolicited basis, to a limited number of investors who represented that they are accredited investors.

Item 3. Defaults Upon Senior Securities.

In the three-month period ended March 31, 2008, and subsequent period through the date hereof, we did not default upon any senior securities.

Item 4. Submission of Matters to a Vote of Security Holders.

In the three-month period ended March 31, 2008, and subsequent period through the date hereof, the we did not submit any matters to a vote of our stockholders:

Item 5. Other Information.

There was no information we were required to disclose in a report on Form 8-K during the three-month period ended March 31, 2008, or subsequent period through the date hereof, which was not so reported.

Item 6. Exhibits

Exhibit No.	Description of Exhibit
31.1	Certification of principal executive officer pursuant to Section 13a-14(a) — filed herewith
31.2	Certification of principal financial and accounting officer pursuant to Section 13a-14(a) — filed herewith
32.1	Certification of principal executive officer pursuant to Section 1350 — filed herewith

32.2 Certification of principal financial and accounting officer pursuant to Section 1350 — filed herewith

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

CHINA SKY ONE MEDICAL, INC.

Dated: May 12, 2008	By:	/s/ Liu Yan-Qing Liu Yan-Qing President and Chief Executive Officer
Dated: May 12, 2008	By:	/s/ Liao Xiaoqing Liao Xiaoqing Chief Financial Officer, Secretary