

CHINA JO-JO DRUGSTORES, INC.
Form 10-Q
February 14, 2019

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, DC 20549

FORM 10-Q

Quarterly Report Pursuant to Section 13 or 15(D) of the Securities Exchange Act of 1934

For the quarterly period ended **December 31, 2018**

or

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: **001-34711**

CHINA JO-JO DRUGSTORES, INC.

(Exact name of registrant as specified in its charter)

Nevada **98-0557852**
(State or other jurisdiction of (I.R.S. Employer
incorporation or organization) Identification No.)

Hai Wai Hai Tongxin Mansion Floor 6

Gong Shu District, Hangzhou City **310008**

Zhejiang Province

P. R. China
(Address of principal executive offices) (Zip Code)

+86 (571) 88077078

(Registrant's telephone number, including area code)

N/A

(Former name, former address and former fiscal year, if changed since last report)

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 No

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 (Sec. 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 No

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

Large Accelerated Filer Accelerated Filer
Non-accelerated filer (Do not check if a smaller reporting company) Smaller reporting company
Emerging growth company

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If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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

As of February 14, 2019, the registrant had 28,936,778 shares of common stock, par value \$0.001 per share, outstanding.

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FOR THE QUARTER ENDED December 31, 2018

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CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING INFORMATION

All statements contained in this Quarterly Report on Form 10-Q (“Form 10-Q”) for the registrant, other than statements of historical facts, that address future activities, events or developments are forward-looking statements, including, but not limited to, statements containing the words “believe,” “anticipate,” “expect” and words of similar import. These statements are based on certain assumptions and analyses made by us in light of our experience and our assessment of historical trends, current conditions and expected future developments as well as other factors we believe are appropriate under the circumstances. However, whether actual results will conform to the expectations and predictions of management is subject to a number of risks and uncertainties that may cause actual results to differ materially.

Such risks include, among others, the following: national and local general economic and market conditions; our ability to sustain, manage or forecast our growth; raw material costs and availability; new product development and introduction; existing government regulations and changes in, or the failure to comply with, government regulations; adverse publicity; competition; the loss of significant customers or suppliers; fluctuations and difficulty in forecasting operating results; changes in business strategy or development plans; business disruptions; the ability to attract and retain qualified personnel; the ability to protect technology; and other factors referenced in this and previous filings.

Consequently, all of the forward-looking statements made in this Form 10-Q are qualified by these cautionary statements and there can be no assurance that the actual results anticipated by management will be realized or, even if substantially realized, that they will have the expected consequences to or effects on our business operations.

PART I - FINANCIAL INFORMATION**ITEM 1. FINANCIAL STATEMENTS****CHINA JO-JO DRUGSTORES, INC. AND SUBSIDIARIES****CONDENSED CONSOLIDATED BALANCE SHEETS**

(UNAUDITED)

| | December 31, 2018 | March 31, 2018 |
|---|----------------------|----------------------|
| <u>ASSETS</u> | | |
| CURRENT ASSETS | | |
| Cash | \$ 5,619,051 | \$ 15,132,640 |
| Restricted cash | 14,988,478 | 16,319,551 |
| Financial assets available for sale | 176,560 | 175,140 |
| Notes receivable | 296,687 | 279,082 |
| Trade accounts receivable | 10,637,316 | 8,322,393 |
| Inventories | 10,483,059 | 13,429,568 |
| Other receivables, net | 3,718,546 | 3,098,079 |
| Advances to suppliers | 3,489,010 | 3,447,452 |
| Other current assets | 1,468,188 | 2,116,237 |
| Total current assets | 50,876,895 | 62,320,142 |
| PROPERTY AND EQUIPMENT, net | 8,427,870 | 2,843,640 |
| OTHER ASSETS | | |
| Long-term investment | 34,208 | 40,890 |
| Farmland assets | 727,064 | 796,286 |
| Long term deposits | 2,266,420 | 2,501,968 |
| Other noncurrent assets | 1,121,814 | 1,253,352 |
| Intangible assets, net | 3,570,986 | 4,056,414 |
| Total other assets | 7,720,492 | 8,648,910 |
| Total assets | \$ 67,025,257 | \$ 73,812,692 |
| LIABILITIES AND STOCKHOLDERS' EQUITY | | |
| CURRENT LIABILITIES | | |
| Accounts payable, trade | 19,223,835 | 25,259,526 |

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| | | |
|--|------------|------------|
| Notes payable | 25,271,064 | 19,180,200 |
| Other payables | 3,851,366 | 4,272,523 |
| Other payables - related parties | 726,219 | 850,342 |
| Customer deposits | 1,492,122 | 4,040,867 |
| Taxes payable | 745,518 | 366,040 |
| Accrued liabilities | 1,618,006 | 841,993 |
| Total current liabilities | 52,928,130 | 54,811,491 |
| Financial liability | 79,957 | |
| Purchase option and warrants liability | 312,751 | 138,796 |
| Total liabilities | 53,320,838 | 54,950,287 |

COMMITMENTS AND CONTINGENCIES

STOCKHOLDERS' EQUITY

| | | |
|--|---------------|--------------|
| Common stock; \$0.001 par value; 250,000,000 shares authorized; 28,936,778 and 28,936,778 shares issued and outstanding as of December 31, 2018 and March 31, 2018 | 28,937 | 28,937 |
| Preferred stock; \$0.001 par value; 10,000,000 shares authorized; nil issued and outstanding as of December 31, 2018 and March 31, 2018 | - | - |
| Additional paid-in capital | 43,747,589 | 43,599,089 |
| Statutory reserves | 1,309,109 | 1,309,109 |
| Accumulated deficit | (33,572,688) | (29,661,190) |
| Accumulated other comprehensive income | 2,628,814 | 3,586,460 |
| Total stockholders' equity | 14,141,761 | 18,862,405 |
| Noncontrolling interests | (437,342) | - |
| Total equity | 13,704,419 | 18,862,405 |
| Total liabilities and stockholders' equity | \$67,025,257 | \$73,812,692 |

The accompanying notes are an integral part of these condensed consolidated financial statements.

CHINA JO-JO DRUGSTORES, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME (LOSS)
(UNAUDITED)

| | For the three months ended December 31, | | For the nine months ended December 31, | |
|---|--|----------------|---|----------------|
| | 2018 | 2017 | 2018 | 2017 |
| REVENUES, NET | \$30,916,549 | \$26,812,242 | \$81,098,161 | \$71,973,653 |
| COST OF GOODS SOLD | 23,780,763 | 21,240,629 | 62,548,471 | 56,666,782 |
| GROSS PROFIT | 7,135,786 | 5,571,613 | 18,549,690 | 15,306,871 |
| SELLING EXPENSES | 6,688,577 | 5,020,971 | 16,539,078 | 13,288,602 |
| GENERAL AND ADMINISTRATIVE EXPENSES | 2,572,862 | 2,737,782 | 6,342,874 | 7,318,780 |
| TOTAL OPERATING EXPENSES | 9,261,439 | 7,758,753 | 22,881,952 | 20,607,382 |
| LOSS FROM OPERATIONS | (2,125,653) | (2,187,140) | (4,332,262) | (5,300,511) |
| INTEREST INCOME | 18,964 | 76,266 | 92,196 | 479,509 |
| OTHER INCOME, NET | 32,795 | 301,292 | 12,436 | 263,241 |
| CHANGE IN FAIR VALUE OF DERIVATIVE LIABILITIES | (85,115) | 221,859 | (173,955) | 420,610 |
| LOSS BEFORE INCOME TAXES | (2,159,009) | (1,587,723) | (4,401,585) | (4,137,151) |
| PROVISION FOR INCOME TAXES | 47,958 | 38,106 | 104,712 | 76,691 |
| NET LOSS | (2,206,967) | (1,625,829) | (4,506,297) | (4,213,842) |
| OTHER COMPREHENSIVE (LOSS) INCOME | | | | |
| Foreign currency translation adjustments | (130,619) | 588,543 | (957,646) | 1,680,796 |
| COMPREHENSIVE LOSS | \$(2,337,586) | \$(1,037,286) | \$(5,463,943) | \$(2,533,046) |
| WEIGHTED AVERAGE NUMBER OF SHARES: | | | | |
| Basic | 28,936,778 | 25,214,678 | 28,936,778 | 25,214,678 |
| Diluted | 28,936,778 | 25,214,678 | 28,936,778 | 25,214,678 |

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EARNINGS PER SHARES:

| | | | | | | | | |
|---------|----------|---|----------|---|----------|---|----------|---|
| Basic | \$ (0.06 |) | \$ (0.08 |) | \$ (0.14 |) | \$ (0.17 |) |
| Diluted | \$ (0.06 |) | \$ (0.08 |) | \$ (0.14 |) | \$ (0.17 |) |

The accompanying notes are an integral part of these condensed consolidated financial statements.

CHINA JO-JO DRUGSTORES, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(UNAUDITED)

| | Nine months ended December 31, | |
|---|-----------------------------------|----------------|
| | 2018 | 2017 |
| CASH FLOWS FROM OPERATING ACTIVITIES: | | |
| Net loss | \$(4,506,297) | \$(4,213,842) |
| Adjustments to reconcile net loss to net cash used in operating activities: | | |
| Bad debt direct write-off and provision | 1,266,994 | 1,948,887 |
| Depreciation and amortization | 937,268 | 1,063,170 |
| Impairment of leasehold improvement | - | (362,737) |
| Stock based compensation | 121,547 | 976,816 |
| Change in fair value of purchase option derivative liability | 173,955 | (420,610) |
| Accounts receivable, trade | (4,061,698) | (4,830,933) |
| Notes receivable | (43,024) | 79,250 |
| Inventories and biological assets | 1,828,232) | (2,945,926) |
| Other receivables | (681,667) | (149,447) |
| Advances to suppliers | (911,061) | (990,309) |
| Other current assets | 476,909 | 562,148 |
| Long term deposit | 18,548 | (1,345,486) |
| Other noncurrent assets | 23,206 | (63,263) |
| Accounts payable, trade | (3,945,980) | 853,598 |
| Other payables and accrued liabilities | 815,725 | (127,969) |
| Customer deposits | (2,258,202) | 387,458 |
| Taxes payable | 422,665 | (222,207) |
| Net cash used in operating activities | (10,322,880) | (9,801,402) |
| CASH FLOWS FROM INVESTING ACTIVITIES: | | |
| Disposal of financial assets available for sale | 87,471 | - |
| Purchase of financial assets available for sale | (104,577) | (136,074) |
| Acquisition of equipment | (5,368,240) | (237,108) |
| Increase in construction-in-progress | - | (1,125,110) |
| Increase intangible assets | (29,879) | - |
| Investment in a joint venture | - | (9,601) |
| Additions to leasehold improvements | (1,432,060) | (249,097) |
| Net cash used in investing activities | (6,847,285) | (1,756,990) |
| CASH FLOWS FROM FINANCING ACTIVITIES: | | |
| Proceeds from notes payable | 32,903,549 | 28,352,683 |

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| | | |
|--|--------------|--------------|
| Repayment of notes payable | (24,930,903) | (22,501,743) |
| Increase in financial liability | 82,167 | - |
| Proceeds from equity and debt financing | 7,544 | - |
| Repayment of other payables-related parties | (82,866) | (278,691) |
| Net cash used in financing activities | 7,979,491 | 5,572,249 |
| | | |
| EFFECT OF EXCHANGE RATE ON CASH | (1,653,988) | 2,408,839 |
| | | |
| INCREASE IN CASH AND CASH EQUIVALENTS AND RESTRICTED CASH | (10,844,662) | (3,577,304) |
| | | |
| CASH AND CASH EQUIVALENTS AND RESTRICTED CASH, beginning of year | 31,452,191 | 27,795,810 |
| | | |
| CASH AND CASH EQUIVALENTS AND RESTRICTED CASH, end of period | \$20,607,529 | \$24,218,506 |
| | | |
| SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION: | | |
| Cash paid for income taxes | \$56,539 | \$27,856 |

The accompanying notes are an integral part of these condensed consolidated financial statements.

Note 1 – DESCRIPTION OF BUSINESS AND ORGANIZATION

China Jo-Jo Drugstores, Inc. (“Jo-Jo Drugstores” or the “Company”), was incorporated in Nevada on December 19, 2006, originally under the name “Kerrisdale Mining Corporation”. On September 24, 2009, the Company changed its name to “China Jo-Jo Drugstores, Inc.” in connection with a share exchange transaction as described below.

On September 17, 2009, the Company completed a share exchange transaction with Renovation Investment (Hong Kong) Co., Ltd. (“Renovation”), whereby 7,900,000 shares of common stock were issued to the stockholders of Renovation in exchange for 100% of the capital stock of Renovation. The completion of the share exchange transaction resulted in a change of control. The share exchange transaction was accounted for as a reverse acquisition and recapitalization and, as a result, the consolidated financial statements of the Company (the legal acquirer) are, in substance, those of Renovation (the accounting acquirer), with the assets and liabilities, and revenues and expenses, of the Company being included effective from the date of the share exchange transaction. Renovation has no substantive operations of its own except for its holdings of Zhejiang Jiuxin Investment Management Co., Ltd. (“Jiuxin Management”), Zhejiang Shouantang Medical Technology Co., Ltd. (“Shouantang Technology”), Hangzhou Jiutong Medical Technology Co., Ltd (“Jiutong Medical”), and Hangzhou Jiuyi Medical Technology Co. Ltd. (“Jiuyi Technology”), its wholly-owned subsidiaries.

The Company is an online and offline retailer and wholesale distributor of pharmaceutical and other healthcare products in the People’s Republic of China (“China” or the “PRC”). The Company’s offline retail business is comprised primarily of pharmacies, which are operated by Hangzhou Jiuzhou Grand Pharmacy Chain Co., Ltd. (“Jiuzhou Pharmacy”), a company that the Company controls through contractual arrangements. On March 31, 2017, Jiuxin Management established a subsidiary, Lin’ An Jiuzhou Pharmacy Co., Ltd (“Lin’ An Jiuzhou”) to operate drugstores in Lin’an City. As of December 31, 2018, Jiuzhou Pharmacy has established the following companies, each of which operates a drugstore in Hangzhou City:

| Entity Name | Date Established |
|---|------------------|
| Hangzhou Jiuben Pharmacy Co., Ltd (“Jiuben Pharmacy”) | April 27, 2017 |
| Hangzhou Jiuli Pharmacy Co., Ltd (“Jiuli Pharmacy”) | May 22, 2017 |
| Hangzhou Jiuxiang Pharmacy Co., Ltd (“Jiuxiang Pharmacy”) | May 26, 2017 |
| Hangzhou Jiuheng Pharmacy Co., Ltd (“Jiuheng Pharmacy”) | June 6, 2017 |
| Hangzhou Jiujiu Pharmacy Co., Ltd (“Jiujiu Pharmacy”) | June 8, 2017 |
| Hangzhou Jiuyi Pharmacy Co., Ltd (“Jiuyi Pharmacy”) | June 8, 2017 |

| | |
|--|-----------------------|
| Hangzhou Jiuyuan Pharmacy Co., Ltd (“Jiuyuan Pharmacy”) | July 13, 2017 |
| Hangzhou Jiumu Pharmacy Co., Ltd (“Jiumu Pharmacy”) | July 21, 2017 |
| Hangzhou Jiurui Pharmacy Co., Ltd (“Jiurui Pharmacy”) | August 4, 2017 |
| Zhejiang Jiuzhou Linjia Medical Investment and Management Co. Ltd (“Linjia Medical”) | September 27, 2017 |

During the nine month period ending December 31, 2018, the Company opened two new stores. All of the new stores were without government insurance reimbursement certificates at their openings.

The Company’s offline retail business also includes three medical clinics through Hangzhou Jiuzhou Clinic of Integrated Traditional and Western Medicine (“Jiuzhou Clinic”) and Hangzhou Jiuzhou Medical and Public Health Service Co., Ltd. (“Jiuzhou Service”), both of which are also controlled by the Company through contractual arrangements. On December 18, 2013, Jiuzhou Service established, and held 51% of, Hangzhou Shouantang Health Management Co., Ltd. (“Shouantang Health”), a PRC company licensed to sell health care products. Shouantang Health was closed in April 2015. In May 2016, Hangzhou Shouantang Bio-technology Co., Ltd. (“Shouantang Bio”) set up and held 49% of Hangzhou Kahamadi Bio-technology Co., Ltd. (“Kahamadi Bio”), a joint venture specialized in brand name development for nutritional supplements. In 2018, Jiuzhou Pharmacy invested a total of \$741,540 (5,100,000RMB) in and held 51% of Zhejiang Jiuzhou Linjia Medical Investment and Management Co. Ltd (“Linjia Medical”), which opened nine new clinics in Hangzhou as of December 31, 2018.

The Company currently conducts its online retail pharmacy business through Jiuzhou Pharmacy, which holds the Company’s online pharmacy license. Prior to November 2015, the Company primarily conducted its online retail pharmacy business through Zhejiang Quannuo Internet Technology Co., Ltd.. In May 2015, the Company established Zhejiang Jianshun Network Technology Co. Ltd, a joint venture with Shanghai Jianbao Technology Co., Ltd. (“Jianshun Network”), in order to develop its online pharmaceutical sales from large commercial medical insurance companies. On September 10, 2015, Renovation set up a new entity Jiuyi Technology to provide additional technical support such as webpage development to our online pharmacy business. In November 2015, the Company sold all of the equity interests of Quannuo Technology to six individuals for approximately \$17,121 (RMB107,074). After the sale, its technical support function has been transferred back to Jiuzhou Pharmacy, which hosts our online pharmacy.

The Company’s wholesale business is primarily conducted through Zhejiang Jiuxin Medicine Co., Ltd. (“Jiuxin Medicine”), which is licensed to distribute prescription and non-prescription pharmaceutical products throughout China. Jiuzhou Pharmacy acquired Jiuxin Medicine on August 25, 2011. On April 20, 2018, 10% of Jiuxin Medicine shares were sold to Hangzhou Kangzhou Biotech Co. Ltd. for a total proceeds of \$79,625 (RMB 507,760),

The Company's herb farming business is conducted by Hangzhou Qianhong Agriculture Development Co., Ltd. ("Qianhong Agriculture"), a wholly-owned subsidiary of Jiuxin Management, which operates a cultivation project of herbal plants used for traditional Chinese medicine ("TCM").

The accompanying consolidated financial statements reflect the activities of the Company and each of the following entities:

| Entity Name | Background | Ownership |
|-----------------------|---|-------------------------------------|
| Renovation | Incorporated in Hong Kong SAR on September 2, 2008 | 100% |
| Jiuxin Management | Established in the PRC on October 14, 2008 Deemed a wholly foreign owned enterprise ("WFOE") under PRC law Registered capital of \$14.5 million fully paid | 100% |
| Shouantang Technology | Established in the PRC on July 16, 2010 by Renovation with registered capital of \$20 million Registered capital requirement reduced by the SAIC to \$11 million in July 2012 and is fully paid Deemed a WFOE under PRC law Invests and finances the working capital of Quannuo Technology | 100% |
| Qianhong Agriculture | Established in the PRC on August 10, 2010 by Jiuxin Management Registered capital of RMB 10 million fully paid Carries out herb farming business | 100% |
| Jiuzhou Pharmacy (1) | Established in the PRC on September 9, 2003 Registered capital of RMB 5 million fully paid | VIE by contractual arrangements (2) |

Operates the “Jiuzhou Grand Pharmacy” stores in Hangzhou

Jiuzhou Clinic (1) Established in the PRC as a general partnership on October 10, 2003 VIE by contractual arrangements (2)

Operates a medical clinic adjacent to one of Jiuzhou Pharmacy’s stores

Jiuzhou Service (1) Established in the PRC on November 2, 2005 VIE by contractual arrangements (2)

Registered capital of RMB 500,000 fully paid

Operates a medical clinic adjacent to one of Jiuzhou Pharmacy’s stores

Established in PRC on December 31, 2003

Jiuxin Medicine Acquired by Jiuzhou Pharmacy in August 2011 VIE by contractual arrangements as a controlled subsidiary of Jiuzhou Pharmacy (2)

Registered capital of RMB 10 million fully paid

Carries out pharmaceutical distribution services

| Entity Name | Background | Ownership |
|-------------------|--|--|
| Jiutong Medical | Established in the PRC on December 20, 2011 by Renovation | Registered capital of \$2.6 million fully paid 100% |
| | Currently has no operation | |
| | Established in the PRC on April 27, 2017 by Jiuzhou Pharmacy | |
| Jiuben Pharmacy | Registered capital of \$15,920 fully paid | VIE by contractual arrangements as a wholly-owned subsidiary of Jiuzhou Pharmacy (2) |
| | Operates a pharmacy in Hangzhou | |
| | Established in the PRC on May 22, 2017 by Jiuzhou Pharmacy | |
| Jiuli Pharmacy | Registered capital of \$15,920 fully paid | VIE by contractual arrangements as a wholly-owned subsidiary of Jiuzhou Pharmacy (2) |
| | Operates a pharmacy in Hangzhou | |
| | Established in the PRC on May 26, 2017 by Jiuzhou Pharmacy | |
| Jiuxiang Pharmacy | Registered capital of \$15,920 fully paid | VIE by contractual arrangements as a wholly-owned subsidiary of Jiuzhou Pharmacy (2) |
| | Operates a pharmacy in Hangzhou | |

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Jiuheng Pharmacy Established in the PRC on June 6, 2017 VIE by contractual arrangements as a wholly-owned subsidiary of Jiuzhou Pharmacy (2)
by Jiuzhou Pharmacy

Registered capital of \$15,920 fully paid

Operates a pharmacy in Hangzhou

Established in the PRC on June 8, 2017
by Jiuzhou Pharmacy

Jiujiu Pharmacy VIE by contractual arrangements as a wholly-owned subsidiary of Jiuzhou Pharmacy (2)
Registered capital of \$15,920 fully paid

Operates a pharmacy in Hangzhou

Established in the PRC on June 8, 2017
by Jiuzhou Pharmacy

Jiuyi Pharmacy VIE by contractual arrangements as a wholly-owned subsidiary of Jiuzhou Pharmacy (2)
Registered capital of \$15,920 fully paid

Operates a pharmacy in Hangzhou

Established in the PRC on July 13, 2017
by Jiuzhou Pharmacy

Jiuyuan Pharmacy VIE by contractual arrangements as a wholly-owned subsidiary of Jiuzhou Pharmacy (2)
Registered capital of \$15,920 fully paid

Operates a pharmacy in Hangzhou

Jiumu Pharmacy Established in the PRC on July 21, 2017 VIE by contractual arrangements as a wholly-owned subsidiary of Jiuzhou Pharmacy (2)
by Jiuzhou Pharmacy

Registered capital of \$15,920 fully paid

Operates a pharmacy in Hangzhou

| Entity Name | Background | Ownership |
|---------------------|---|---|
| | Established in the PRC on August, 2017 by Jiuzhou Pharmacy | |
| Jiurui Pharmacy | Registered capital of \$15,920 fully paid | VIE by contractual arrangements as a wholly-owned subsidiary of Jiuzhou Pharmacy (2) |
| | Operates a pharmacy in Hangzhou | |
| | Established in the PRC in October, 2014 by Shouantang Technology | |
| | 100% held by Shouantang Technology | |
| Shouantang Bio | Registered capital of RMB 1,000,000 fully paid | 100% |
| | Sells nutritional supplements under its own brand name | |
| | Established in the PRC on September 10, 2015 | |
| Jiuyi Technology | 100% held by Renovation | 100% |
| | Technical support to online pharmacy | |
| Kahamadi Bio | Established in the PRC in May 2016 | 49% |
| | 49% held by Shouantang Bio | |

Registered capital of RMB 10 million

Develop brand name for nutritional supplements

Established in the PRC on March 31, 2017

100% held by Jiuxin Management

Lin'An Jiuzhou

100%

Registered capital of RMB 5 million

Explore retail pharmacy market in Lin'An City

Established in the PRC on September 27, 2017

51% held by Jiuzhou Pharmacy

Linjia Medical

VIE by contractual arrangements as a controlled subsidiary of Jiuzhou Pharmacy (2)

Registered capital of RMB 20 million

Operates local clinics

Jiuzhou Pharmacy, Jiuzhou Clinic and Jiuzhou Service had been under the common control of Mr. Lei Liu, Mr. Chong'an Jin and Ms. Li Qi, the three shareholders of Renovation (the "Owners") since their respective establishment dates, pursuant to agreements among the Owners to vote their interests in concert as memorialized in a voting (1) rights agreement. Based on such voting agreement, the Company has determined that common control exists among these three companies. The Owners have operated these three companies in conjunction with one another since each company's respective establishment date. Jiuxin Medicine is also deemed under the common control of the Owners as a subsidiary of Jiuzhou Pharmacy.

(2) To comply with certain foreign ownership restrictions of pharmacy and medical clinic operators, Jiuxin Management entered into a series of contractual arrangements with Jiuzhou Pharmacy, Jiuzhou Clinic and Jiuzhou Service on August 1, 2009. These contractual arrangements are comprised of five agreements: a consulting services agreement, operating agreement, equity pledge agreement, voting rights agreement and option agreement. Because such agreements obligate Jiuxin Management to absorb all of the risks of loss from the activities of

Jiuzhou Pharmacy, Jiuzhou Clinic and Jiuzhou Service, and enable the Company (through Jiuxin Management) to receive all of their expected residual returns, the Company accounts for each of the three companies (as well as subsidiaries of Jiuzhou Pharmacy) as a variable interest entity (“VIE”) under the accounting standards of the Financial Accounting Standards Board (“FASB”). Accordingly, the financial statements of Jiuzhou Pharmacy, Jiuzhou Clinic and Jiuzhou Service, as well as the subsidiary under the control of Jiuzhou Pharmacy, Jiuxin Medicine and Shouantang Bio are consolidated into the financial statements of the Company.

Note 2 – LIQUIDITY

Our accounts have been prepared in accordance with U.S. GAAP on a going concern basis. The going concern basis assumes that assets are realized and liabilities are extinguished in the ordinary course of business at amounts disclosed in the financial statements. Our ability to continue as a going concern depends upon aligning our sources of funding (debt and equity) with our expenditure requirements and repayment of the short-term debts as and when they become due.

The drug retail business is a highly competitive industry in PRC. Several large drugstore chains and a variety of single stores operate in Hangzhou City and Zhejiang Province. In order to increase our competitive advantages and gain more local retail pharmacy market share, during fiscal year 2018, we opened 57 new stores in Hangzhou. As a result, we incurred significant expenses related to rent, hiring and training employees, and marketing activities. As the retail pharmaceutical market has become more competitive in recent years, a new store is generally not profitable in its first year of operation. In fact, we incurred significant expense with limited incremental revenue in the period we opened new stores.

As of December 31, 2018, all but 43 of the new stores have not obtained government insurance reimbursement certificates. It usually takes more than one year for a new store to apply for and obtain the local government insurance reimbursement certificate. Historically, sales reimbursed from the government insurance agency accounts for more than half of total revenue in a mature store. We are actively in the process of applying for certificates for all of our new stores. As more and more new stores obtain certificates, we expect our new store revenue will increase and eventually contribute positive operating cash flow.

The Company's principal sources of liquidity consist of existing cash, equity financing, bank facilities from local banks as well as personal loans from its principal shareholders if necessary. On January 23, 2017, we completed a private placement with a single healthcare-focused institutional investor for the purchase of an aggregate of 4,840,000 shares of our common stock at a price of \$2.20 per share and received gross proceeds of approximately \$10,648,000. The Company has two credit line agreements from a local bank as displayed in detail in Note 14. Approximately \$2.39 million bank credit line was still available for further borrowing as of December 31, 2018. Any borrowing therefrom is guaranteed by a third-party guarantor company, and secured by the Company's assets pursuant to a collateral agreement, as well as the personal guarantees of some of its principal shareholders.

However, in the event the banks withdraw their credit lines with us, or our existing store performance suddenly deteriorates due to unexpected government policy changes, or our operating license is canceled as a result of violation of industry regulations, the Company may or may not be able to obtain alternative financing resources to support its continuing operation. At that time, the Company may not be able to continue to present itself on a going concern basis.

Note 3 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of presentation and consolidation

The accompanying consolidated financial statements are prepared in accordance with accounting principles generally accepted in the United States of America (“US GAAP”). The consolidated financial statements include the financial statements of the Company, its wholly-owned subsidiaries and VIEs. All significant inter-company transactions and balances between the Company, its subsidiaries and VIEs are eliminated upon consolidation.

Consolidation of variable interest entities

In accordance with accounting standards regarding consolidation of variable interest entities, VIEs are generally entities that lack sufficient equity to finance their activities without additional financial support from other parties or whose equity holders lack adequate decision making ability. All VIEs with which the Company is involved must be evaluated to determine the primary beneficiary of the risks and rewards of the VIE. The primary beneficiary is required to consolidate the VIE for financial reporting purposes.

The Company has concluded, based on the contractual arrangements, that Jiuzhou Pharmacy (including its subsidiaries and controlled entities), Jiuzhou Clinic and Jiuzhou Service are each a VIE and that the Company’s wholly-owned subsidiary, Jiuxin Management, absorbs a majority of the risk of loss from the activities of these companies, thereby enabling the Company, through Jiuxin Management, to receive a majority of their respective expected residual returns.

Additionally, as Jiuzhou Pharmacy, Jiuzhou Clinic and Jiuzhou Service are under common control, the consolidated financial statements have been prepared as if the transactions had occurred retroactively as to the beginning of the reporting period of these consolidated financial statements.

Control and common control are defined under the accounting standards as “an individual, enterprise, or immediate family members who hold more than 50 percent of the voting ownership interest of each entity.” Because the Owners collectively own 100% of Jiuzhou Pharmacy, Jiuzhou Clinic and Jiuzhou Service, and have agreed to vote their interests in concert since the establishment of each of these three companies as memorialized in the voting rights agreement, the Company believes that the Owners collectively have control and common control of the three companies. Accordingly, the Company believes that Jiuzhou Pharmacy, Jiuzhou Clinic and Jiuzhou Service were

constructively held under common control by Jiuxin Management as of the time the Contractual Agreements were entered into, establishing Jiuxin Management as their primary beneficiary. Jiuxin Management, in turn, is owned by Renovation, which is owned by the Company.

Risks and Uncertainties

The operations of the Company are located in the PRC. Accordingly, the Company's business, financial condition, and results of operations may be influenced by the political, economic, and legal environments in the PRC, as well as by the general state of the PRC economy. The Company's operations in the PRC are subject to special considerations and significant risks not typically associated with companies in North America and Western Europe. These include risks associated with, among others, the political, economic and legal environment and foreign currency exchange. The Company's results may be adversely affected by changes in the political, regulatory and social conditions in the PRC. Although the Company has not experienced losses from these situations and believes that it is in compliance with existing laws and regulations including its organization and structure disclosed in Note 1, this may not be indicative of future results.

The Company has significant cash deposits with suppliers in order to obtain and maintain inventory. The Company's ability to obtain products and maintain inventory at existing and new locations is dependent upon its ability to post and maintain significant cash deposits with its suppliers. In the PRC, many vendors are unwilling to extend credit terms for product sales and instead require cash deposits to be made. The Company does not generally receive interest on any of its supplier deposits, and such deposits are subject to loss as a result of the creditworthiness or bankruptcy of the party who holds such funds, as well as the risk from illegal acts such as conversion, fraud, theft or dishonesty associated with the third party. If these circumstances were to arise, the Company would find it difficult or impossible, due to the unpredictability of legal proceedings in China, to recover all or a portion of the amount on deposit with its suppliers.

Members of the current management team own controlling interests in the Company and are also the Owners of the VIEs in the PRC. The Company only controls the VIEs through contractual arrangements which obligate it to absorb the risk of loss and to receive the residual expected returns. As such, the controlling shareholders of the Company and the VIEs may cancel these agreements or permit them to expire at the end of the agreement terms, as a result of which the Company would not retain control of the VIEs.

Use of estimates

The preparation of unaudited condensed consolidated financial statements in conformity with US GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. The significant estimates made in the preparation of the accompanying unaudited condensed consolidated financial statements relate to the assessment of the carrying values of accounts receivable, advances to suppliers and related allowance for doubtful accounts, useful lives of property and equipment, inventory reserve and fair value of its purchase option derivative liability. Because of the use of estimates inherent in the financial reporting process, actual results could materially differ from those estimates.

Fair value measurements

The Company has adopted FASB ASC Topic 820, “Fair Value Measurement and Disclosure,” which defines fair value, establishes a framework for measuring fair value in GAAP, and expands disclosures about fair value measurements. It does not require any new fair value measurements, but provides guidance on how to measure fair value by providing a fair value hierarchy used to classify the source of the information. It establishes a three-level valuation hierarchy of valuation techniques based on observable and unobservable inputs, which may be used to measure fair value and include the following:

Level 1 – Quoted prices in active markets for identical assets or liabilities.

Level 2 – Inputs other than Level 1 that are observable, either directly or indirectly, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

Level 3 – Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

Classification within the hierarchy is determined based on the lowest level of input that is significant to the fair value measurement.

The Company's financial assets and liabilities, which include financial instruments as defined by FASB ASC 820, include cash and cash equivalents, accounts receivable, accounts payable, long-term debt and derivatives. The carrying amounts of cash and cash equivalents, financial assets available for sales, accounts receivable, notes receivables, and accounts payable are a reasonable approximation of fair value due to the short maturities of these instruments (Level 1). The carrying amount of notes payable approximates fair value based on borrowing rates of similar bank loan currently available to the Company (Level 2) (See Note 14). The carrying amount of the Company's derivative instruments is recorded at fair value and is determined based on observable inputs that are corroborated by market data (Level 2). As of December 31, 2018, the fair values of our derivative instruments that were carried at fair value (See Note 18 and 19).

| | Active Market for Identical Assets (Level 1) | Observable Inputs (Level 2) | Unobservable Inputs (Level 3) | Total Carrying Value |
|---------------------------|--|-----------------------------------|-------------------------------------|----------------------------|
| Cash and cash equivalents | 5,619,051 | - | \$ - | 5,619,051 |
| Restricted Cash | 14,988,478 | | | 14,988,478 |
| Notes payable | - | 25,271,064 | - | 25,271,064 |
| Financial liability | | | 79,957 | 79,957 |
| Warrants liability | - | 312,751 | \$ - | 312,751 |
| Total | 20,607,529 | 25,583,815 | \$ 79,957 | 46,271,301 |

Revenue recognition

Revenue from sales of prescription medicine at drugstores is recognized when the prescription is filled and the customer picks up and pays for the prescription.

Revenue from sales of other merchandise at drugstores is recognized at the point of sale, which occurs when a customer pays for and receives the merchandise. Usually the majority of our merchandise, such as prescription and OTC drugs, are not allowed to be returned after the customers leave the counter. Return of other products, such as sundry products, are minimal. Sales of drugs reimbursed by the local government medical insurance agency and receivables from the agency are recognized when a customer pays for the drugs at a store. Based on historical experience, a reserve for potential loss from denial of reimbursement on certain unqualified drugs is made to the

receivables from the government agency.

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Revenue from medical services is recognized after the service has been rendered to a customer.

Revenue from online pharmacy sales is recognized when merchandise is shipped to customers. While most deliveries take one day, certain deliveries may take longer depending on a customer's location. Any loss caused in a shipment will be reimbursed by the Company's courier company. Our sales policy allows for the return of certain merchandises without reason within seven days after customer's receipt of the applicable merchandise. A proper sales reserve is made to account for the potential loss from returns from customers. Historically, sales returns seven days after merchandise receipts have been minimal.

Revenue from sales of merchandise to non-retail customers is recognized when the following conditions are met: (1) persuasive evidence of an arrangement exists (sales agreements and customer purchase orders are used to determine the existence of an arrangement); (2) delivery of goods has occurred and risks and benefits of ownership have been transferred, which is when the goods are received by the customer at its designated location in accordance with the sales terms; (3) the sales price is fixed or determinable; and (4) collectability is probable. Historically, sales returns have been minimal.

The Company's revenue is net of value added tax ("VAT") collected on behalf of PRC tax authorities in respect to the sales of merchandise. VAT collected from customers, net of VAT paid for purchases, is recorded as a liability in the accompanying consolidated balance sheets until it is paid to the relevant PRC tax authorities.

Restricted cash

The Company's restricted cash consists of cash and long-term deposits in a bank as security for its notes payable. The Company has notes payable outstanding with the bank and is required to keep certain amounts on deposit that are subject to withdrawal restrictions. The notes payable are generally short term in nature due to their short maturity period of six to nine months; thus, restricted cash is classified as a current asset.

Accounts receivable

Accounts receivable represents the following: (1) amounts due from banks relating to retail sales that are paid or settled by the customers' debit or credit cards, (2) amounts due from government social security bureaus and commercial health insurance programs relating to retail sales of drugs, prescription medicine, and medical services that are paid or settled by the customers' medical insurance cards, (3) amounts due from non-bank third party payment

instruments such as Alipay and certain e-commerce platforms and (4) amounts due from non-retail customers for sales of merchandise.

Accounts receivable are recorded at net realizable value consisting of the carrying amount less an allowance for uncollectible accounts, as necessary. In the Company's retail business, accounts receivable mainly consist of reimbursements due from the government insurance bureaus and commercial health insurance programs and are usually collected within two or three months. The Company directly writes off delinquent account balances, which it determines to be uncollectible after confirming with the appropriate bureau or program each month. Additionally, the Company also makes estimated reserves on related outstanding accounts receivable based on historical trends.

In the Company's online pharmacy business, accounts receivable primarily consist of amounts due from non-bank third party payment instruments such as Alipay and certain e-commerce platforms. To purchase pharmaceutical products from an e-commerce platforms such as Tmall, customers are required to submit payment to certain non-bank third party payment instruments, such as Alipay, which, in turn, reimburse the Company within seven days to a month. Except for customer returns of sold products, the receivables from these payments instruments are rarely uncollectible.

In its wholesale business, the Company uses the aging method to estimate the allowance for anticipated uncollectible receivable balances. Under the aging method, bad debt percentages are determined by management, based on historical experience and the current economic climate, are applied to customers' balances categorized by the number of months the underlying invoices have remained outstanding. At each reporting period, the allowance balance is adjusted to reflect the amount computed as a result of the aging method. When facts subsequently become available to indicate that the allowance provided requires an adjustment, a corresponding adjustment is made to the allowance account as a change in estimate.

Advances to suppliers

Advances to suppliers consist of prepayments to our vendors, such as pharmaceutical manufacturers and other distributors. Since the acquisition of Jiuxin Medicine, we have transferred almost all logistics services of our retail drugstores to Jiuxin Medicine. Jiuzhou Pharmacy only directly purchases certain non-medical products, such as certain nutritional supplements. As a result, almost all advances to suppliers are made by Jiuxin Medicine.

Advances to suppliers for our drug wholesale business consist of prepayments to our vendors, such as pharmaceutical manufacturers and other distributors. We typically receive products from vendors within three to nine months after making prepayments. We continuously monitor delivery from, and payments to, our vendors while maintaining a provision for estimated credit losses based upon historical experience and any specific supplier issues, such as discontinuing of inventory supply, that have been identified. If we have difficulty receiving products from a vendor, we take the following steps: cease purchasing products from such vendor, ask for return of our prepayment promptly, and if necessary, take legal action. If all of these steps are unsuccessful, management then determines whether the

prepayments should be reserved or written off.

Inventories

Inventories are stated at the lower of cost or market value. Cost is determined using the first in first out (FIFO) method. Market value is the lower of replacement cost or net realizable value. The Company carries out physical inventory counts on a monthly basis at each store and warehouse location. Herbs that the Company farms are recorded at their cost, which includes direct costs such as seed selection, fertilizer, labor costs that are spent in growing herbs on the leased farmland, and indirect costs such as amortization of farmland development cost. All costs are accumulated until the time of harvest and then allocated to harvested herbs costs when the herbs are sold. The Company periodically reviews its inventory and records write-downs to inventories for shrinkage losses and damaged merchandise that are identified. The Company provides a reserve for estimated inventory obsolescence or excess quantities on hand equal to the difference, if any, between the cost of the inventory and its estimated realizable value.

Farmland assets

Herbs that the Company farms are recorded at their cost, which includes direct costs such as seed selection, fertilizer, and labor costs that are spent in growing herbs on the leased farmland, and indirect costs such as amortization of farmland development costs. Since April 2014, amortization of farmland development costs has been expensed instead of allocated into inventory due to unpredictable future market value of planted ginkgo trees.

All related costs described in the above are accumulated until the time of harvest and then allocated to harvested herbs when they are sold.

Property and equipment

Property and equipment are stated at cost, net of accumulated depreciation or amortization. Depreciation is calculated on the straight-line method over the estimated useful lives of the assets, taking into consideration the assets' estimated residual value. Leasehold improvements are amortized over the shorter of lease term or remaining lease period of the underlying assets. Following are the estimated useful lives of the Company's property and equipment:

| | Estimated Useful Life |
|------------------------------|-----------------------|
| Leasehold improvements | 3-10 years |
| Motor vehicles | 3-5 years |
| Office equipment & furniture | 3-5 years |

Buildings 35 years

Maintenance, repairs and minor renewals are charged to expenses as incurred. Major additions and betterment to property and equipment are capitalized.

Intangible assets

Intangible assets are acquired individually or as part of a group of assets, and are initially recorded at their fair value. The cost of a group of assets acquired in a transaction is allocated to the individual assets based on their relative fair values.

The estimated useful lives of the Company's intangible assets are as follows:

| | Estimated Useful Life |
|-----------------|--------------------------|
| Land use rights | 50 years |
| Software | 3 years |

The Company evaluates intangible assets for impairment whenever events or changes in circumstances indicate that the assets might be impaired.

Impairment of long lived assets

The Company evaluates long lived tangible and intangible assets for impairment, whenever events or changes in circumstances indicate that the carrying value may not be recoverable from its estimated future cash flows. Recoverability is measured by comparing the assets' net book value to the related projected undiscounted cash flows from these assets, considering a number of factors including past operating results, budgets, economic projections, market trends and product development cycles. If the net book value of the asset exceeds the related undiscounted cash flows, the asset is considered impaired, and a second test is performed to measure the amount of impairment loss. There were no fixed assets and farmland assets impaired for the three and nine months ended December 31, 2018.

Notes payable

During the normal course of business, the Company regularly issues bank acceptance bills as a payment method to settle outstanding accounts payables with various material suppliers. The Company records such bank acceptance bills as notes payable. Such notes payable are generally short term in nature due to their short maturity period of six to nine months.

Income taxes

The Company follows FASB ASC Topic 740, "Income Taxes," which requires the recognition of deferred tax assets and liabilities for the expected future tax consequences of events that have been included in the financial statements or tax returns. Under this method, deferred income taxes are recognized for the tax consequences in future years of differences between the tax bases of assets and liabilities and their financial reporting amounts at each period end based on enacted tax laws and statutory tax rates, applicable to the periods in which the differences are expected to affect taxable income. Valuation allowances are established, when necessary, to reduce deferred tax assets to the amount expected to be realized.

The Company has adopted FASB ASC Topic 740-10-25, which provides criteria for the recognition, measurement, presentation and disclosure of uncertain tax position. The Company must recognize the tax benefit from an uncertain tax position only if it is more likely than not that the tax position will be sustained on examination by the taxing authorities, based on the technical merits of the position. The tax benefits recognized in the financial statements from such a position are measured based on the largest benefit that has a greater than 50% likelihood of being realized upon ultimate resolution. The Company performed a self-assessment and the Company's liability for income taxes includes liability for unrecognized tax benefits, interest and penalties which relate to tax years still subject to review by taxing authorities. Audit periods remain open for review until the statute of limitations has passed, which in the PRC is usually 5 years. The completion of review or the expiration of the statute of limitations for a given audit period could result in an adjustment to the Company's liability for income taxes. Any such adjustment could be material to the Company's results of operations for any given quarterly or annual period based, in part, upon the results of operations for the given period. As of September 30, 2018 and March 31, 2018, the management of the Company considered that the Company had no additional liabilities for uncertain tax positions affecting its consolidated financial position and results of operations or cash flows, and will continue to evaluate for any uncertain position in the future. There are no estimated interest costs and penalties provided in the Company's consolidated financial statements for the three months ended September 30, 2018 and 2017, respectively. The Company's tax positions related to open tax years are subject to examination by the relevant tax authorities, the most significant of which is the China Tax Authority.

Value added tax

Sales revenue represents the invoiced value of goods, net of VAT. All of the Company's products are sold in the PRC and are subject to a VAT on the gross sales price. Since April 2018, The VAT rates have been adjusted to range up to 16%, depending on the type of products sold. The VAT may be offset by VAT paid by the Company on raw materials and other materials included in the cost of producing or acquiring its finished products. The Company recorded a VAT payable net of payments in the accompanying financial statements.

The accounting standards clarify the accounting and disclosure requirements for uncertain tax positions and prescribe a recognition threshold and measurement attribute for recognition and measurement of a tax position taken or expected to be taken in a tax return. The accounting standards also provide guidance on de-recognition, classification, interest and penalties, accounting in interim periods, disclosures, and transition. No significant penalties, uncertain tax provisions or interest relating to income taxes were incurred during the periods ended December 31, 2018 and 2017.

Stock based compensation

The Company follows the provisions of FASB ASC 718, "Compensation — Stock Compensation," which establishes accounting standards for non-employee and employee stock-based awards. Under the provisions of FASB ASC 718, the fair value of stock issued is used to measure the fair value of services received as the Company believes such approach is a more reliable method of measuring the fair value of the services. For non-employee stock-based awards, fair value is measured based on the value of the Company's common stock on the date that the commitment for performance by the counterparty has been reached or the counterparty's performance is complete. The fair value of the equity instrument is calculated and then recognized as compensation expense over the requisite performance period. For employee stock-based awards, share-based compensation cost is measured at the grant date based on the fair value of the award and is recognized as expense with graded vesting on a straight-line basis over the requisite service period for the entire award.

Advertising and promotion costs

Advertising and promotion costs are expensed as incurred and amounted to \$259,064 and \$197,326 for the three months ended December 31, 2018 and 2017, respectively, and \$657,968 and \$518,060 for the nine months ended December 31, 2018 and 2017, respectively. Such costs consist primarily of print and promotional materials such as flyers to local communities.

Operating leases

The Company leases premises for retail drugstores, offices and wholesale warehouse under non-cancellable operating leases. Operating lease payments are expensed over the term of lease. A majority of the Company's retail drugstore leases have a 3 to 10 year term with a renewal option upon the expiration of the lease; the wholesale warehouse lease has a 10-year term with a renewal option upon the expiration of the lease. The Company has historically been able to renew a majority of its drugstores leases. Under the terms of the lease agreements, the Company has no legal or contractual asset retirement obligations at the end of the lease. In addition, land leased from the government is amortized on a straight-line basis over a 30-year term.

Foreign currency translation

The Company uses the United States dollar (“U.S. dollars” or “USD”) for financial reporting purposes. The Company’s subsidiaries and VIEs maintain their books and records in their functional currency the Renminbi (“RMB”), the currency of the PRC.

In general, for consolidation purposes, the Company translates the assets and liabilities of its subsidiaries and VIEs into U.S. dollars using the applicable exchange rates prevailing at the balance sheet date, and the statements of income and cash flows are translated at average exchange rates during the reporting period. As a result, amounts related to assets and liabilities reported on the statement of cash flows will not necessarily agree with changes in the corresponding balances on the balance sheet. Equity accounts are translated at historical rates. Adjustments resulting from the translation of the financial statements of the subsidiaries and VIEs are recorded as accumulated other comprehensive income.

The balance sheet amounts, with the exception of equity, at December 31, 2018 and at March 31, 2018 were translated at 1 RMB to 0.1454 USD and at 1 RMB to 0.1592 USD, respectively. The average translation rates applied to income and cash flow statement amounts for the nine months ended December 31, 2018 and 2017 were at 1 RMB to 0.1494 USD and at 1 RMB to 0.1512 USD, respectively.

Concentrations and credit risk

Certain financial instruments, which subject the Company to concentration of credit risk, consist of cash and restricted cash. The Company has cash balances at financial institutions located in Hong Kong and PRC. Balances at financial institutions in Hong Kong may, from time to time, exceed Hong Kong Deposit Protection Board’s insured limits. Since March 31, 2015, balances at financial institutions and state-owned banks within the PRC are insured up to RMB 500,000 (USD 75,916) per bank. As of December 31, 2018 and March 31, 2018, the Company had deposits totaling \$20,593,311 and \$31,433,969 that were covered by such limited insurance, respectively. Any balance over RMB 500,000 (USD 75,916) per bank in PRC will not be covered. To date, the Company has not experienced any losses in such accounts.

For the three months ended December 31, 2018, three largest vendors accounted for 70.3% of the Company’s total purchases and one vendor accounted for 32.6% of the Company’s total advances to suppliers. For the three months ended December 31, 2017, three largest vendors accounted for 31.0% of the Company’s total purchases and one vendor accounted for 13.6% of the Company’s total advances to suppliers.

For the nine months ended December 31, 2018, two vendors accounted for 46.9% of the Company's total purchases and two vendors accounted for more than 10% of total advances to suppliers. For the nine months ended December 31, 2017, the Company's two largest vendors accounted for 26.1% of the Company's total purchases and one vendor accounted for 18.1% of the Company's total advances to suppliers.

For the three months and nine months ended December 31, 2018, no customer accounted for more than 10% of the Company's total sales and more than 10% of total accounts receivable. For the three months and six months ended December 31, 2017, no customer accounted for more than 10% of the Company's total sales or more than 10% of total accounts receivable.

Recent Accounting Pronouncements

In February 2016, the FASB issued No. 2016-02 "Leases (Topic 842): Increasing transparency and comparability among organizations by recognizing lease assets and lease liabilities on the balance sheet and disclosing key information about leasing arrangements." The amendments in this update are effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years, for any of the following: 1. A public business entity; 2. A not-for-profit entity that has issued, or is a conduit bond obligor for, securities that are traded, listed, or quoted on an exchange or an over-the-counter market; 3. An employee benefit plan that files financial statements with the U.S. Securities and Exchange Commission (SEC). For all other entities, the amendments in this update are effective for fiscal years beginning after December 15, 2019, and interim periods within fiscal years beginning after December 15, 2020. Early application of the amendments in this update is permitted for all entities. We are currently evaluating the impact of the adoption of ASU 2016-02 on our consolidated financial statements.

In June 2016, the FASB issued ASU 2016-13, “Financial Instruments—Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments,” providing financial statement users with more decision-useful information about the expected credit losses on financial instruments and other commitments to extend credit held by a reporting entity at each reporting date. For public business entities that are U.S. Securities and Exchange Commission (SEC) filers, the amendments in this update are effective for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years. All entities may adopt the amendments in this update earlier as of the fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. We are currently evaluating the impact of the adoption of ASU 2016-13 on our consolidated financial statements.

In August 2016, the FASB issued ASU 2016-15, “Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments,” addressing eight specific cash flow issues with the objective of reducing the existing diversity in practice. The amendments in this update are effective for public business entities for fiscal years beginning after December 15, 2017, and interim periods within those fiscal years. Early adoption is permitted, including adoption in an interim period. If an entity early adopts the amendments in an interim period, any adjustments should be reflected as of the beginning of the fiscal year that includes that interim period. An entity that elects early adoption must adopt all of the amendments in the same period. The amendments in this update should be applied using a retrospective transition method to each period presented. If it is impracticable to apply the amendments retrospectively for some of the issues, the amendments for those issues would be applied prospectively as of the earliest date practicable. The impact of adoption on its Condensed Consolidated Financial Statements for any period presented is not material.

In July 2017, the FASB issued Accounting Standards update (“ASU”) No. 2017-11, “Earnings Per Share (Topic 260), Distinguishing Liabilities from Equity (Topic 480), Derivatives and Hedging (Topic 815): I. Accounting for Certain Financial Instruments with Down Round Features; II. Replacement of the Indefinite Deferral for Mandatorily Redeemable Financial Instruments of Certain Nonpublic Entities and Certain Mandatorily Redeemable Noncontrolling Interests with a Scope Exception”. Part I of this update addresses the complexity of accounting for certain financial instruments with down round features. Part II of this update addresses the difficulty of navigating Topic 480, Distinguishing Liabilities from Equity, because of the existence of extensive pending content in the FASB Accounting Standards Codification®. We are currently evaluating the impact of the adoption of ASU 2017-11 on our consolidated financial statements.

In January 2017, the FASB issued Accounting Standards update (“ASU”) No. 2017-04, “Intangibles—Goodwill and Other (Topic 350): Simplifying the Test for Goodwill Impairment” (“ASU 2017-04”), which removes Step 2 from the goodwill impairment test. An entity will apply a one-step quantitative test and record the amount of goodwill impairment as the excess of a reporting unit’s carrying amount over its fair value, not to exceed the total amount of goodwill allocated to the reporting unit. The new guidance does not amend the optional qualitative assessment of goodwill impairment. Public business entity that is a U.S. Securities and Exchange Commission filer should adopt the amendments in this ASU for its annual or any interim goodwill impairment test in fiscal years beginning after December 15, 2019. Early adoption is permitted for interim or annual goodwill impairment tests performed on testing dates after January 1, 2017. We are currently evaluating the impact of the adoption of ASU 2017-04 on our consolidated financial statements.

In February 2018, the FASB released ASU 2018-2, “Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income.” This standard update addresses a specific consequence of the Tax Cuts and Jobs Act (“U.S. tax reform”) and allows a reclassification from accumulated other comprehensive income to retained earnings for the stranded tax effects resulting from U.S. tax reform. Consequently, the update eliminates the stranded tax effects that were created as a result of the historical U.S. federal corporate income tax rate to the newly enacted U.S. federal corporate income tax rate. The Company is required to adopt this standard in the first quarter of fiscal year 2021, with early adoption permitted. The amendments in this update should be applied either in the period of adoption or retrospectively to each period in which the effect of the change in the U.S. federal corporate income tax rate in the Tax Cuts and Jobs Act is recognized. We are currently evaluating the impact of adoption on its Condensed Consolidated Financial Statements.

Adoption of New Revenue Recognition Standard

In May 2014, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) 2014-09, Revenue from Contracts with Customers (Topic 606). ASU 2014-09 outlines a single comprehensive model for companies to use in accounting for revenue arising from contracts with customers and supersedes most current revenue recognition guidance, including industry-specific guidance. In March 2016, the FASB issued ASU 2016-08, “Principal Versus Agent Considerations (Reporting Revenue Gross Versus Net),” which amends the principal versus-agent implementation guidance and in April 2016 the FASB issued ASU 2016-10, “Identifying Performance Obligations and Licensing,” which amends the guidance in those areas in the new revenue recognition standard. On April 1, 2018, we adopted the guidance in ASC 606 and all the related amendments and applied the new revenue standard to all contracts using the modified retrospective method. Based on the new standard our revenue recognition policies related to membership rewards programs will change. But the impact of the new revenue standard was not material and there was no adjustment required to the opening balance of retained earnings. We expect the impact of the adoption of the new revenue standard to be immaterial to our net income on an ongoing basis.

The following is a discussion of the Company's revenue recognition policies by segment under the new revenue recognition accounting standard:

Pharmacy retail sales

The physical pharmacies sell prescription drugs, OTC drugs, traditional Chinese medicine, nutritional supplements, medical devices and sundry products. Revenue from sales of prescription medicine at drugstores is recognized when the prescription is filled and the customer picks up and pays for the prescription. Revenue from sales of other merchandise at drugstores is recognized at the point of sale, which is when a customer pays for and receives the merchandise. Usually the majority of our merchandise, such as prescription and OTC drugs, are not allowed to be returned after the customers leave the counter. Return of other products, such as sundry products, are minimal. Sales of drugs reimbursed by the local government medical insurance agency and receivables from the agency are recognized when a customer pays for the drugs at a store. Based on historical experience, a reserve for potential loss from denial of reimbursement on certain unqualified drugs is made to the receivables from the government agency. Revenue from medical services is recognized after the service has been rendered to a customer. As revenue from medical services are minimal compared to pharmacy retail sales, it is included as part of the pharmacy retail sales.

Online pharmacy sales

The online pharmacy sells various health products except for prescription drugs. Revenue from online pharmacy sales is recognized when merchandise is shipped to customers. While most deliveries take one day, certain deliveries may take longer depending on a customer's location. Any loss caused in a shipment will be reimbursed by the Company's courier company. Our sales policy allows for the return of certain merchandises without reason within seven days after customer's receipt of the applicable merchandise. A proper sales reserve is made to account for the potential loss from returns from customers. Historically, sales returns seven days after merchandise receipts have been minimal.

Wholesale

Jiuxin Medicine purchases medicine in quantity and distributes products primarily to local pharmacies and medical products dealers. Revenue from sales of merchandise to non-retail customers is recognized when the following conditions are met: (1) persuasive evidence of an arrangement exists (sales agreements and customer purchase orders are used to determine the existence of an arrangement); (2) delivery of goods has occurred and risks and benefits of ownership have been transferred, which is when the goods are received by the customer at its designated location in accordance with the sales terms; (3) the sales price is fixed or determinable; and (4) collectability is probable. Historically, sales returns have been minimal.

The Company's revenue is net of value added tax ("VAT") collected on behalf of PRC tax authorities in respect to the sales of merchandise. VAT collected from customers, net of VAT paid for purchases, is recorded as a liability in the accompanying consolidated balance sheets until it is paid to the relevant PRC tax authorities.

Disaggregation of Revenue

The following table disaggregates the Company's revenue by major source in each segment for the three and nine months ended December 31, 2018:

| Three months ended December 31 | 2018 | 2017 |
|--------------------------------|--------------|--------------|
| Retail drugstores | | |
| Prescription drugs | \$6,756,073 | \$5,373,870 |
| OTC drugs | 9,393,148 | 9,168,708 |
| Nutritional supplements | 1,869,351 | 1,883,020 |
| TCM | 1,342,768 | 1,185,004 |
| Sundry products | 248,729 | 180,338 |
| Medical devices | 1,257,180 | 497,282 |
| Total retail revenue | \$20,867,249 | \$18,288,222 |
| Online pharmacy | | |
| Prescription drugs | \$- | \$- |
| OTC drugs | 837,126 | 1,535,383 |
| Nutritional supplements | 220,776 | 514,952 |
| TCM | 28,785 | 8,802 |
| Sundry products | 573,993 | 224,514 |
| Medical devices | 832,526 | 1,111,396 |
| Total online revenue | \$2,493,206 | \$3,395,047 |
| Drug wholesale | | |
| Prescription drugs | \$3,933,441 | \$2,777,566 |
| OTC drugs | 3,341,676 | 2,303,726 |
| Nutritional supplements | 167,069 | 19,123 |
| TCM | 77,216 | 20,876 |
| Sundry products | 5,949 | - |
| Medical devices | 30,743 | 7,682 |
| Total wholesale revenue | \$7,556,094 | \$5,128,973 |
| Total revenue | \$30,916,549 | \$26,812,242 |

| Nine months ended December 31 | 2018 | 2017 |
|-------------------------------|--------------|--------------|
| Retail drugstores | | |
| Prescription drugs | \$17,835,700 | \$14,860,659 |
| OTC drugs | 24,018,263 | 21,593,385 |
| Nutritional supplements | 4,750,013 | 4,558,383 |
| TCM | 4,615,033 | 3,136,203 |
| Sundry products | 799,554 | 804,817 |
| Medical devices | 2,953,326 | 1,402,760 |
| Total retail revenue | \$54,971,889 | \$46,356,207 |
| Online pharmacy | | |
| Prescription drugs | \$- | \$- |
| OTC drugs | 2,412,057 | 4,038,674 |
| Nutritional supplements | 575,862 | 1,365,834 |
| TCM | 54,417 | 18,984 |
| Sundry products | 2,128,282 | 1,065,935 |
| Medical devices | 1,467,304 | 3,106,325 |
| Total online revenue | \$6,637,922 | \$9,595,752 |
| Drug wholesale | | |
| Prescription drugs | \$11,708,683 | \$9,252,199 |
| OTC drugs | 7,246,356 | 6,652,879 |
| Nutritional supplements | 240,666 | 47,660 |
| TCM | 156,525 | 21,480 |
| Sundry products | 21,479 | - |
| Medical devices | 114,641 | 47,476 |
| Total wholesale revenue | \$19,488,350 | \$16,021,694 |
| Total revenue | \$81,098,161 | \$71,973,653 |

Contract Balances

Contract liabilities primarily represent the Company's obligation to transfer additional goods or services to a customer for which the Company has received consideration, for example membership points. The consideration received remains a contract liability until goods or services have been provided to the retail customer.

The following table provides information about receivables and contract liabilities from contracts with customers:

| | December 31, 2018 | March 31, 2018 |
|--|----------------------|-------------------|
| Trade receivable(included in accounts receivable, net) | \$ 10,637,316 | \$8,322,393 |
| Contract liabilities (included in accrued expenses) | 2,196,478 | 4,461,136 |

Impact of New Revenue Recognition Standard on Financial Statement Line Items

The Company adopted ASU 2014-09 using the modified retrospective method. The cumulative effect of applying the new guidance to all contracts was recorded as an adjustment to retained earnings as of the adoption date. As a result of applying the modified retrospective method to adopt the new revenue guidance, the following adjustments were made to accounts on the condensed statement of operation for the three and nine months ended December 31, 2018:

| In thousands | Impact of Change in Accounting Policy | | |
|---|---|-------------|---------------------------------------|
| | As Reported Balances For the Three Months Ended December 31, 2018 | Adjustments | Balance without Adoption of Topic 606 |
| Condensed Consolidated Statement of Operations: | | | |
| Net revenues | 30,916 | (36) | 30,880 |
| Cost of revenues | 23,780 | - | 23,776 |
| Gross profit | 7,135 | (36) | 7,099 |
| SELLING EXPENSES | 6,688 | 36 | 6,724 |
| GENERAL AND ADMINISTRATIVE EXPENSES | 2,572 | - | 2,572 |
| Operating profit | (2,125) | - | (2,125) |
| Income (loss) before income tax provision | (2,159) | - | (2,159) |
| Income tax provision | 47 | - | 47 |
| Income (loss) from continuing operations | (2,206) | - | (2,206) |
| Net income (loss) | (2,206) | - | (2,206) |

| In thousands | Impact of Change in Accounting Policy | | |
|--|--|-------------------|---------------------------------------|
| | As Reported Balances For the Nine Months Ended | December 31, 2018 | Adjustments |
| | | | Balance without Adoption of Topic 606 |
| Condensed Consolidated Statement of Operations: | | | |
| Net revenues | 81,098 | 106 | 81,024 |
| Cost of revenues | 62,548 | - | 62,548 |
| Gross profit | 18,550 | 106 | 18,656 |
| SELLING EXPENSES | 16,539 | (106) | 16,433 |
| GENERAL AND ADMINISTRATIVE EXPENSES | 6,342 | - | 6,342 |
| Operating profit | (4,332) | - | (4,332) |
| Income (loss) before income tax provision | (4,401) | - | (4,401) |
| Income tax provision | 104 | - | 104 |
| Income (loss) from continuing operations | (4,506) | - | (4,506) |
| Net income (loss) | (4,506) | - | (4,506) |

The adoption of ASU 2014-09 has no effect on consolidated balance sheet and statement of cash flow.

Adoption of Statement of Cash Flows

In November 2016, the FASB issued ASU 2016-18, Statement of Cash Flows, which amends Accounting Standard Codification (“ASC”) Topic 230. This ASU requires entities to show the changes in the total of cash, cash equivalents, restricted cash and restricted cash equivalents in the statement of cash flows. When cash, cash equivalents, restricted cash and restricted cash equivalents are presented in more than one line item on the balance sheet, the new guidance requires a reconciliation of the totals in the statement of cash flows to the related captions in the balance sheet. Entities will also have to disclose the nature of their restricted cash and restricted cash equivalent balances. The guidance is required to be applied retrospectively. The Company adopted this new accounting guidance. The following represents a reconciliation of cash and cash equivalents in the condensed consolidated balance sheet to total cash, cash equivalents and restricted cash in the condensed consolidated statement of cash flows:

December 31, March 31,

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| | 2018 | 2018 |
|---|------------|------------|
| Cash and cash equivalents | 5,619,051 | 15,132,640 |
| Restricted cash | 14,988,478 | 16,319,551 |
| Total cash, cash equivalents and restricted cash in the statement of cash flows | 20,607,529 | 31,452,191 |

Restricted cash in the condensed consolidated balance sheets primarily represents deposits required by a bank as security for its notes payable. The Company has notes payable outstanding with the bank and is required to keep certain amounts on deposit that are subject to withdrawal restrictions. All restricted cash is invested in time deposits and money markets, which are classified within Level 1 of the fair value hierarchy.

Restricted cash activity was previously reported in “Change in restricted cash” within financing activities cash flows on the Company’s condensed consolidated statement of cash flows. The following is a reconciliation of the effect on the relevant line items on the statement of cash flows for the nine months ended December 31, 2017 as a result of adopting this new accounting guidance:

| | As Previously Reported | Adjustments | As Revised |
|--|------------------------------|-------------|---------------|
| Nine Months Ended December 31, 2017 | | | |
| Change in restricted cash | -5,743,155 | 5,743,155 | - |
| Net cash provided by financing activities | -170,906 | 5,743,155 | 5,572,249 |
| Effects of exchange rate on cash | 1,760,935 | 647,905 | 2,408,840 |
| Net decrease in cash, cash equivalents and restricted cash | -9,968,364 | 6,391,060 | -3,577,304 |
| Cash, cash equivalents, and restricted cash at the beginning of the period | 18,364,424 | 9,431,386 | 27,795,810 |
| Cash, cash equivalents, and restricted cash at the end of the period | 8,396,060 | 15,822,446 | 24,218,506 |

Note 4 – FINANCIAL ASSETS AVAILABLE FOR SALE

As of December 31, 2018 and March 31, 2018, financial assets available for sale amounted to \$176,560 (RMB1,214,500) and \$175,140 (RMB 1,100,000), respectively. In the year ended March 31, 2018, the Company invested a total of \$159,915 as a limited partner (LP) in a private equity fund (PE fund), which is intended to invest in retail pharmaceutical business. However, as the PE fund has not been able to use its proceeds, it agreed to refund \$85,118 (RMB585,000) as of December 31, 2018. Additionally, the Company has signed an investment agreement with Inter Mongolia Songlu Pharmaceutical Co.(“Songlu Pharmaceutical”) and invested a total of \$87,225 (RMB600,000), which accounts for 0.5% shares of Songlu Pharmaceutical. The Company has also invested in a mutual fund a total of \$14,538 (RMB100,000), which can be liquidated by giving notice.

Note 5 – TRADE ACCOUNTS RECEIVABLE

Trade accounts receivable consisted of the following:

| | December 31, 2018 | March 31, 2018 |
|---------------------------------------|----------------------|-------------------|
| Accounts receivable | \$ 15,489,718 | \$ 12,883,707 |
| Less: allowance for doubtful accounts | (4,852,402) | (4,561,314) |
| Trade accounts receivable, net | \$ 10,637,316 | \$ 8,322,393 |

For the three months ended December 31, 2018 and 2017, \$36,077 and \$33,738 in accounts receivable were directly written off respectively. For the nine months ended December 31, 2018 and 2017, \$64,412 and \$158,721 in accounts receivable were directly written off, respectively. As of December 31, 2018 and March 31, 2018, no trade accounts receivables were pledged as collateral for borrowings from financial institutions.

Note 6 – OTHER CURRENT ASSETS

Other current assets consisted of the following:

| | December 31, 2018 | March 31, 2018 |
|--|----------------------|-------------------|
| Prepaid rental expenses ⁽¹⁾ | \$ 1,285,752 | \$1,984,856 |
| Prepaid and other current assets | 182,436 | 131,381 |
| Total | \$ 1,468,188 | \$2,116,237 |

(1) Represents store and office rental expenses that were usually prepaid and amortized over the prepayment period.

Note 7 – PROPERTY AND EQUIPMENT

Property and equipment consisted of the following:

| | December 31, 2018 | March 31, 2018 |
|--------------------------------|----------------------|-------------------|
| Building* | \$6,280,935 | \$1,707,145 |
| Leasehold improvements | 8,338,779 | 7,606,496 |
| Farmland development cost | 1,738,621 | 1,904,151 |
| Office equipment and furniture | 5,252,629 | 5,581,554 |
| Motor vehicles | 579,891 | 456,442 |
| Total | 22,190,875 | 17,255,788 |
| Less: Accumulated depreciation | (11,474,422) | (11,905,893) |
| Impairment** | (2,288,583) | (2,506,255) |
| Property and equipment, net | \$8,427,870 | \$2,843,640 |

The increase of property and equipment from March 31, 2018 to December 31, 2018 is due to the purchase of

* Yueming shop, a new store which cost \$4,722,193 (RMB32,482,394). The new store is located downtown south Hangzhou and adjacent to a super shopping mall. The Company plans to create a new flagship store.

** The variance of impairment from March 31, 2018 to December 31, 2018 is solely caused by exchange rate variance.

Depreciation expenses for property and equipment totaled \$338,946 and \$406,048 for the three months ended December 31, 2018 and 2017, respectively. Depreciation expenses for property and equipment totaled \$770,919 and \$982,202 for the nine months ended December 31, 2018 and 2017, respectively. There were no fixed assets impaired in the three and nine months ended December 31, 2018.

Note 8 – ADVANCES TO SUPPLIERS

Advances to suppliers consist of deposits, with or advances to, outside vendors for future inventory purchases. Most of the Company's suppliers require a certain amount of money to be deposited with them as a guarantee that the Company will receive its purchase on a timely basis. This amount is refundable and bears no interest. As of December 31, 2018 and March 31, 2018, advance to suppliers consist of the following:

| | December 31, 2018 | March 31, 2018 |
|---|----------------------|-------------------|
| Advance to suppliers* | \$ 6,826,569 | \$ 6,505,545 |
| Less: allowance for unrefundable advances | (3,337,559) | (3,058,092) |
| Advance to suppliers, net | \$ 3,489,010 | \$ 3,447,452 |

* In order to achieve a larger rebate for certain merchandise, such as colla coril asini (donkey-hide gelatin), from certain suppliers, the Company made a significant cash advance to such suppliers.

For the three and nine months ended December 31, 2018 and 2017, none of the advances to suppliers were written off against previous allowance for unrefundable advances, respectively.

Note 9 – INVENTORY

Inventory consisted of finished goods, valued at \$10,483,059 and \$13,429,568 as of December 31, 2018 and March 31, 2018, respectively. The Company constantly monitors its potential obsolete products and is allowed to return products close to their expiration dates to its suppliers. Any loss on damaged items is immaterial and will be recognized immediately. As a result, no reserves were made for inventory as of December 31, 2018 and March 31, 2018.

Note 10 – FARMLAND ASSETS

Farmland assets consist of ginkgo trees planted in 2012 and expected to be harvested and sold in several years. As of December 31, 2018 and March 31, 2018, farmland assets are valued as follows:

| | December 31, 2018 | March 31, 2018 |
|----------------------|----------------------|-------------------|
| Farmland assets | \$ 2,206,741 | \$ 2,416,839 |
| Less: Impairment* | (1,479,677) | (1,620,553) |
| Farmland assets, net | \$ 727,064 | \$ 796,286 |

* The estimated fair value is estimated to be lower than its investment value as of December 31, 2018 and March 31, 2018.

Note 11 – LONG TERM DEPOSITS, LANDLORDS

As of December 31, 2018 and March 31, 2018, long term deposits amounted to \$2,266,420 and \$2,501,968, respectively. Long term deposits are money deposited with, or advanced to, landlords for the purpose of securing retail store leases that the Company does not anticipate being returned within the next twelve months. Most of the Company's landlords require a minimum payment of nine months' rent, paid upfront, plus additional deposits.

Note 12 – OTHER NONCURRENT ASSETS

Other noncurrent assets consisted of the following:

| | December 31, 2018 | March 31, 2018 |
|-------------------------|----------------------|-------------------|
| Forest land use rights* | \$ 1,089,421 | \$ 1,235,253 |
| Others | 32,393 | 18,099 |
| Total | \$ 1,121,814 | \$ 1,253,352 |

* The prepayment for lease of forest land use rights is a payment made to a local government in connection with entering into an operating land lease agreement. The land is currently used to cultivate Ginkgo trees. The forest rights certificate from the local village extends the life of the lease to January 31, 2060.

The amortization of the prepayment for the lease of forest land use right was approximately \$6,812 and \$7,765 for the three months ended December 31, 2018 and 2017, respectively. The amortization of the prepayment for the lease of forest land use right was approximately \$20,487 and \$21,653 for the nine months ended December 31, 2018 and 2017, respectively.

The Company's amortizations of the prepayment for lease of land use right for the next five years and thereafter are as follows:

| For the year ending December 31, | Amount |
|----------------------------------|----------|
| 2019 | \$28,071 |
| 2020 | 28,071 |
| 2021 | 28,071 |

| | |
|------------|---------|
| 2022 | 28,071 |
| 2023 | 28,071 |
| Thereafter | 949,066 |

Note 13 – INTANGIBLE ASSETS

Net intangible assets consisted of the following at:

| | December 31, 2018 | March 31, 2018 |
|--------------------------------|----------------------|-------------------|
| License ⁽¹⁾ | \$ 1,863,603 | \$ 1,967,934 |
| SAP software ⁽²⁾ | 660,010 | 764,104 |
| Land use rights ⁽³⁾ | 1,417,651 | 1,552,622 |
| Total intangible assets | 3,941,264 | 4,284,660 |
| Less: accumulated amortization | (370,279) | (228,246) |
| Intangible assets, net | \$ 3,570,986 | \$ 4,056,414 |

Amortization expense of intangibles amounted to \$50,342 and \$38,412 for the three months ended December 31, 2018 and 2017, respectively, and \$166,349 and \$52,876 for the nine months ended December 31, 2018 and 2017, respectively.

This represents the fair value of the licenses of insurance applicable drugstores acquired from Sanhao Pharmacy, a drugstore chain Jiuzhou Pharmacy acquired in 2014. The licenses allow patients to pay by using insurance cards at stores. The stores are reimbursed from the Human Resource and Social Security Department of Hangzhou City. In September 2017, the Company acquired several new stores for the purpose of the Municipal Social Medical Reimbursement Qualification Certificates. The owners of these acquired drugstores agreed to cease their stores' business and liquidate all of the stores' accounts before Jiuzhou Pharmacy acquired them. As a result, Jiuzhou Pharmacy has not obtained any assets or liabilities from the stores, but was able to transfer the certificates to our new stores opened at the same time.

In 2017, we have installed a leading ERP system, SAP from Germany. SAP is a well-known management system used by many Fortune 500 companies. As of December 31, 2018, the system has been completely installed and has been running for eleven months in the Company. By automatically connecting commodity flow data with accounting recording, the system minimizes the manual errors made by accounting staff. Additionally, the system provides a view of overall and instant cash information by electronically linking local banking systems with SAP. Additional benefits include automatically-generated customized monthly company performance reports, instant inventory monitoring and reporting, and punctual maintenance of customer and supplier accounts.

In July 2013, the Company purchased the land use rights of a plot of farmland in Lin'an, Hangzhou, intended for the establishment of an herb processing plant in the future. However, as our farming business in Lin'an has not grown, the Company does not expect completion of the plant in the near future.

Note 14 – NOTES PAYABLE

The Company has credit facilities with Hangzhou United Bank (“HUB”), Bank of Hangzhou (“BOH”), and China Merchant Bank (“CMB”) that provided working capital in the form of the following bank acceptance notes at December 31, 2018 and March 31, 2018:

| Beneficiary | Endorser | Origination date | Maturity date | December 31, 2018 | March 31, 2018 |
|---------------------------------|----------|------------------|---------------|-------------------|----------------|
| Jiuzhou Pharmacy ⁽¹⁾ | HUB | 10/10/17 | 04/10/18 | | 2,552,769 |
| Jiuzhou Pharmacy ⁽¹⁾ | HUB | 11/24/17 | 05/24/18 | | 21,972 |
| Jiuzhou Pharmacy ⁽¹⁾ | HUB | 12/05/17 | 06/05/18 | | 377,347 |
| Jiuzhou Pharmacy ⁽¹⁾ | HUB | 12/29/17 | 06/29/18 | | 1,194,135 |
| Jiuzhou Pharmacy ⁽¹⁾ | HUB | 12/29/17 | 06/29/18 | | 1,443,554 |
| Jiuzhou Pharmacy ⁽¹⁾ | HUB | 02/05/18 | 08/05/18 | | 2,618,500 |
| Jiuzhou Pharmacy ⁽¹⁾ | HUB | 03/05/18 | 09/05/18 | | 3,072,638 |
| Jiuzhou Pharmacy ⁽¹⁾ | HUB | 11/06/17 | 05/06/18 | | 3,553,014 |
| Jiuzhou Pharmacy ⁽¹⁾ | HUB | 12/05/17 | 06/05/18 | | 1,937,683 |
| Jiuzhou Pharmacy ⁽¹⁾ | HUB | 12/29/17 | 06/29/18 | | 1,687,711 |
| Jiuzhou Pharmacy ⁽¹⁾ | HUB | 11/06/18 | 05/06/19 | 488,767 | - |
| Jiuzhou Pharmacy ⁽¹⁾ | HUB | 12/12/18 | 06/12/19 | 2,182,572 | - |
| Jiuzhou Pharmacy ⁽¹⁾ | HUB | 12/20/18 | 03/20/19 | 110,767 | - |
| Jiuzhou Pharmacy ⁽¹⁾ | HUB | 12/20/18 | 06/20/19 | 1,046,714 | |
| Jiuzhou Pharmacy ⁽¹⁾ | HUB | 12/29/18 | 06/29/19 | 5,372,061 | |
| Jiuzhou Pharmacy ⁽¹⁾ | HUB | 07/05/18 | 01/05/19 | 2,989,780 | |
| Jiuzhou Pharmacy ⁽¹⁾ | HUB | 08/06/18 | 02/06/19 | 1,357,129 | |
| Jiuzhou Pharmacy ⁽¹⁾ | HUB | 08/17/18 | 02/17/19 | 277,657 | |
| Jiuzhou Pharmacy ⁽¹⁾ | HUB | 08/31/18 | 02/28/19 | 2,300,155 | |
| Jiuzhou Pharmacy ⁽¹⁾ | HUB | 09/05/18 | 03/05/19 | 1,876,612 | |
| Jiuxin Medicine ⁽²⁾ | HUB | 10/11/18 | 04/11/19 | 4,353,836 | |
| Jiuxin Medicine ⁽²⁾ | HUB | 11/07/18 | 05/07/19 | 2,915,014 | |
| Jiuxin Medicine ⁽²⁾ | CMB | 02/02/18 | 08/02/18 | | 71,648 |
| Jiuxin Medicine ⁽²⁾ | CMB | 02/07/18 | 08/07/18 | | 95,530 |
| Jiuxin Medicine ⁽²⁾ | CMB | 03/07/18 | 09/07/18 | | 538,857 |
| Jiuxin Medicine ⁽²⁾ | CMB | 03/15/18 | 09/15/18 | | 44,842 |
| Total | | | | \$ 25,271,064 | \$ 19,180,200 |

(1) As of December 31, 2018, the Company had \$25,271,064 (RMB 173,831,238) of notes payable from HUB. The Company is required to hold restricted cash in the amount of \$14,723,476 (RMB 101,277,889) with HUB as collateral against these bank notes. Included in the restricted cash is a total of \$10,194,220 three-year deposit (RMB 70,122,647) deposited into HUB as a collateral for current and future notes payable from HUB. As of March 31, 2018, the Company had \$18,429,322 (RMB 115,748,985) of notes payable from HUB. The Company is required to

hold restricted cash in the amount of \$13,565,300 (RMB 85,199,540) with HUB as collateral against these bank notes. Included in the restricted cash is a total of \$7,269,509 three-year deposit (RMB 45,657,584) deposited into HUB as a collateral for current and future notes payable from HUB.

As of December 31, 2018, the Company had \$0 (RMB0) of notes payable from CMB, with restricted cash in the (2) amount of \$0 (RMB0) held at the bank. As of March 31, 2018, the Company had \$750,878 (RMB 4,716,037) of notes payable from CMB, with restricted cash in the amount of \$750,878 (RMB 4,716,037) held at the bank.

As of December 31, 2018, the Company had a credit line of approximately \$12.94 million in the aggregate from HUB. By putting up a three-year deposit of \$10.19 million and the restricted cash of \$4.53 million deposited in the banks, the total credit line was \$27.66 million. As of December 31, 2018, the Company had approximately \$25.27 million of bank notes payable and approximately \$2.39 million bank credit line was still available for further borrowing. The bank notes are secured by three shops of Jiuzhou Pharmacy and guaranteed by the Company's major shareholders.

Note 15 – TAXESIncome tax

The Company accounts for income taxes under the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax basis, operating losses and tax credit carryforwards. Deferred tax assets and liabilities are calculated using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in the period that includes the enactment date. Valuation allowances are provided against deferred income tax assets for amounts which are not considered “more likely than not” to be realized.

The Company is subject to income taxes on an entity basis on income arising in or derived from the tax jurisdiction in which each entity is domiciled.

| Entity | Income Tax Jurisdiction |
|--------------------|-------------------------|
| Jo-Jo Drugstores | United States |
| Renovation | Hong Kong, PRC |
| All other entities | Mainland, PRC |

For the three and six months ended December 31, 2018 and 2017, the components of income tax expense consist of the following:

| | For the three months ended December 31, | | For the nine months ended December 31, | |
|-----------|---|--------|--|--------|
| | 2018 | 2017 | 2018 | 2017 |
| Current: | | | | |
| Federal | - | - | - | - |
| State | - | - | - | - |
| Foreign | 47,958 | 38,106 | 104,712 | 76,691 |
| | 47,958 | 38,106 | 104,712 | 76,691 |
| Deferred: | | | | |
| Federal | - | - | - | - |

| | | | | |
|----------------------------|--------|--------|---------|--------|
| State | - | - | - | - |
| Foreign | - | - | - | - |
| Provision for income taxes | 47,958 | 38,106 | 104,712 | 76,691 |

The following table reconciles the U.S. statutory tax rates with the Company's effective tax rate for the three and nine months ended December 31, 2018 and 2017:

| | For the three months ended December 31, | | For the nine months ended December 31, | |
|--|---|---------|--|---------|
| | 2018 | 2017 | 2018 | 2017 |
| U.S. Statutory rates | 21.0 % | 34.0 % | 21.0 % | 34.0 % |
| Foreign income not recognized in the U.S. | (21.0) | (34.0) | (21.0) | (34.0) |
| China income taxes | 25.0 | 25.0 | 25.0 | 25.0 |
| Change in valuation allowance (1) | (25.0) | (25.0) | (25.0) | (25.0) |
| Non-deductible expenses-permanent difference (2) | (2.2) | (2.4) | (2.4) | (1.9) |
| Effective tax rate | (2.2)% | (2.4)% | (2.4)% | (1.9)% |

(1) Represents a non-taxable expense due to overall increase in allowance for accounts receivable and advances to suppliers.

(2) The (2.2)% and (2.4)% rate adjustments for the three months ended December 31, 2018 and 2017 and the (2.4)% and (1.9)% rate adjustments for the nine months ended December 31, 2018 and 2017 represent expenses that primarily include stock option expenses and legal, accounting and other expenses incurred by the Company that are not deductible for PRC income tax.

Jo-Jo Drugstores is incorporated in the U.S. and incurred a net operating loss for income tax purposes for the three and nine months ended December 31, 2018 and 2017. As of December 31, 2018, the estimated net operating loss carry forwards for U.S. income tax purposes amounted to \$1,503,000, which may be available to reduce future years' taxable income. These carry forwards will expire if not utilized by 2032. Management believes that the realization of the benefits arising from this loss appears to be uncertain due to the Company's continuing losses for U.S. income tax purposes. Accordingly, the Company has provided a 100% valuation allowance at December 31, 2018. There was no net change in the valuation allowance for the three and nine months ended December 31, 2018 and 2017. Management reviews this valuation allowance periodically and makes adjustments as necessary.

The components of the Company's net deferred tax assets are as follows:

| | As of 12/31/2018 | As of 12/31/2017 |
|--|---------------------|---------------------|
| Allowance | 771,675 | 584,427 |
| Long-lived assets impairment | - | - |
| Depreciation and Amortization | 139,483 | 147,655 |
| Accrued expense | 420,143 | 140,124 |
| Net operating loss carryforward | 2,859,896 | 1,765,468 |
| Foreign Tax Credit Carryover | 195,000 | 195,000 |
| Total deferred tax assets (liabilities): | 4,386,197 | 2,832,673 |
| Valuation allowance | (4,386,197) | (2,832,673) |
| Net deferred tax assets (liabilities) | - | - |

The Company regularly assesses the realizability of its deferred tax assets and establishes a valuation allowance if it is more likely than not that some portion of the deferred tax assets will not be realized. We weigh all available positive and negative evidence, including earnings history and results of recent operations, scheduled reversals of deferred tax liabilities, projected future taxable income, and tax planning strategies. Assumptions used to forecast future taxable income often require significant judgment. More weight is given to objectively verifiable evidence. In the event we determine that we would not be able to realize all or part of our net deferred tax assets in the future, a valuation allowance will be established against deferred tax assets in the period in which we make such determination. The need to establish a valuation allowance against deferred tax assets may cause greater volatility in our effective tax rate.

As of December 31, 2018 and December 31, 2017, the estimated net operating loss carry forwards for U.S. income tax purposes amounted to \$816,908, which may be available to reduce future years' taxable income. These carry forwards will expire if not utilized by 2032. In addition, the Company carries a foreign tax credit of \$195,000. As of December 31, 2018 and December 31, 2017, the estimated net operating loss carry forwards for Hong Kong income tax purposes amounted to \$1,905,689 and \$1,772,884, which may be available to reduce future years' taxable income. As of December 31, 2018 and December 31, 2017, the estimated net operating loss carry forwards for China income tax purposes amounted to \$14,820,829 and \$8,236,919, which may be available to reduce future years' taxable income. These carry forwards will expire if not utilized in next five years.

On December 22, 2017, the U.S. federal government enacted the 2017 Tax Act. The 2017 Tax Act includes a number of changes in existing tax law impacting businesses, including the transition tax, a one-time deemed repatriation of cumulative undistributed foreign earnings and a permanent reduction in the U.S. federal statutory rate from 35% to 21%, effective on January 1, 2018. ASC 740 requires companies to recognize the effect of tax law changes in the period of enactment, accordingly, the effects must be recognized on companies' calendar year-end financial statements, even though the effective date for most provisions is January 1, 2018. As a result, we re-measured our net U.S.

deferred tax assets at the 21% future tax rate. At December 31, 2017, according to the 2017 Tax Act for estimating our foreign undistributed earnings, we estimated an aggregate deficit in “accumulated earnings and profits,” which is how foreign undistributed earnings are determined for the one-time transition tax and for U.S. income tax purposes. As a result, the one-time transition tax did not have a significant impact on the Company’s FY18 tax provision and there was no undistributed accumulated earnings and profits as of September 30, 2018.

In December 2017, the SEC issued Staff Accounting Bulletin No. 118 (“SAB 118”), which provided a measurement period of up to one year from the enactment date of the 2017 Tax Act for us to complete the accounting for the 2017 Tax Act and its related impacts. The income tax effects of the 2017 Tax Act for which the accounting is incomplete include: the impact of the transition tax, the revaluation of deferred tax assets and liabilities to reflect the 21% corporate tax rate, and the impact to the aforementioned items on state income taxes. We have made reasonable provisional estimates for each of these items, however, these estimates may be affected by other analyses related to the 2017 Tax Act, including but not limited to, any deferred adjustments related to the filing of our fiscal 2018 federal and state income tax returns and further guidance yet to be issued.

The Company recorded net unrecognized tax benefits of \$0.0 million as of January 31, 2018. It is our policy to classify accrued interest and penalties related to unrecognized tax benefits in the provision for income taxes.

Audit periods remain open for review until the statute of limitations has passed, which in the PRC, the Company’s most significant tax jurisdiction, is usually 5 years. The completion of review or the expiration of the statute of limitations for a given audit period could result in an adjustment to the Company’s liability for income taxes. Any such adjustment could be material to the Company’s results of operations for any given quarterly or annual period based, in part, upon the results of operations for the given period.

Note 16 – POSTRETIREMENT BENEFITS

Regulations in the PRC require the Company to contribute to a defined contribution retirement plan for all permanent employees. The contribution for each employee is based on a percentage of the employee’s current compensation as required by the local government. The Company contributed \$338,083 and \$312,701 in employment benefits and pension for the three months ended December 31, 2018 and 2017, respectively. The Company contributed \$1,039,163 and \$872,435 in employment benefits and pension for the nine months ended December 31, 2018 and 2017, respectively.

Note 17 – RELATED PARTY TRANSACTIONS AND ARRANGEMENTS

Amounts payable to related parties are summarized as follows:

| | December 31, 2018 | March 31, 2018 |
|--|----------------------|-------------------|
| Due to a director and CEO ⁽¹⁾ : | 726,219 | 850,342 |
| Total | \$ 726,219 | \$ 850,342 |

(1) Due to foreign exchange restrictions, the Company's director and CEO, Mr. Lei Liu personally lent U.S. dollars to the Company to facilitate its payments of expenses in the United States.

As of December 31, 2018 and March 31, 2018, notes payable totaling \$0 and \$3,253,630 were secured by the personal properties of certain of the Company's shareholders, respectively. The lien on such shareholders' properties has been released since July 2018.

The Company leases a retail space from Mr. Lei Liu. The lease expires in September 2020. Rent expenses totaled \$16,136 and \$4,536 for the three months ended December 31, 2018 and 2017, respectively. Rent expenses totaled \$25,100 and \$12,959 for the nine months ended December 31, 2018 and 2017, respectively. All amounts due and payable have been paid to Mr. Liu as of December 31, 2018.

Note 18 – Financial Liability

To encourage operating teams, which consists of doctors and nurses, to devote their efforts to run clinics, Linjia Medical allows them to put deposits in the clinic where doctors and nurses work, and take shares in any profit of the clinic. The principal amounts of the deposits are refundable if the doctors and nurses leave the clinic. In order to properly reflect Linjia Medical's liabilities, the Company reclassifies the deposits of \$79,957 (RMB550,000) as financial liability as of December 31, 2018.

Note 19 – WARRANTS

In connection with the registered direct offering closed on July 19, 2015, the Company issued a warrant to an investor to purchase up to 600,000 shares of common stock at an exercise price of \$3.10 per share. The warrant became exercisable on January 19, 2016 and will expire on January 18, 2021. In connection with the offering, the Company also issued a warrant to its placement agent of this offering, pursuant to which the agent may purchase up to 6% of the aggregate number of shares of common stock sold in the offering, i.e. 72,000 shares. Such warrant has the same terms as the warrant issued to investor in the offering.

The fair value of the warrants issued to purchase 672,000 shares as described above was estimated by using the binominal pricing model with the following assumptions:

| | Common Stock Warrants December 31, 2018 ⁽¹⁾ | Common Stock Warrants March 31, 2018 | | |
|-------------------------|--|--|---|---|
| Stock price | \$ 2.00 | \$ 1.35 | | |
| Exercise price | \$ 3.10 | \$ 3.10 | | |
| Annual dividend yield | 0 | % 0 | % | % |
| Expected term (years) | 2.30 | 2.80 | | |
| Risk-free interest rate | 2.48 | % 1.98 | % | % |
| Expected volatility | 67.70 | % 68.73 | % | % |

(1) As of December 31, 2018, the warrants had not been exercised.

Upon evaluation, as the warrants meet the definition of a derivative under FASB ASC 815, as the Company cannot avoid a net cash settlement under certain circumstances. Accordingly, the fair value of the warrants was classified as a liability of \$138,796 as of March 31, 2018. For the three and nine months ended December 31, 2018, the Company recognized a loss of \$85,116 and \$116,522 for the investor warrant and placement agent warrant, from the change in fair value of the warrant liability. As a result, the warrant liability is carried on the consolidated balance sheets at the fair value of \$312,751 for the investor warrant and placement agent warrant, collectively, as of December 31, 2018.

Note 20 – STOCKHOLDER’S EQUITY

Common stock

On January 23, 2017, the Company closed a private offering with one institutional investor (the “Investor”) pursuant to which the Company sold to the Investor, and the Investor purchased from the Company, an aggregate of 4,840,000 shares of the common stock, par value \$0.001 per share, of the Company, at a purchase price of \$2.20 per share, for aggregate gross proceeds to the Company of \$10,648,000 (the “Private Placement”).

Stock-based compensation

The Company accounts for share-based payment awards granted to employees and directors by recording compensation expense based on estimated fair values. The Company estimates the fair value of share-based payment awards on the date of grant. The value of the portion of the award that is ultimately expected to vest is recognized as an expense over the requisite service periods in the Company’s consolidated statements of operations. Share-based awards are attributed to expenses using the straight-line method over the vesting period. The Company determines the value of each option award that contains a market condition using a Monte Carlo Simulation valuation model, while all other option awards are valued using the Black-Scholes valuation model as permitted under FASB ASC 718 “Compensation - Stock Compensation.” The assumptions used in calculating the fair value of share-based payment awards represent the Company’s best estimates. The Company’s estimates of the fair values of stock options granted and the resulting amounts of share-based compensation recognized may be impacted by certain variables including stock price volatility, employee stock option exercise behaviors, additional stock option modifications, estimates of forfeitures, and the related income tax impact.

On March 30, 2018, the Company granted a total of 3,947,100 shares of restricted common stock to its key employees in its retail drugstores and online pharmacy under the Company’s 2010 Equity Incentive Plan, as amended (the “Plan”). The stock awards vested on the grant date. On June 28, 2018, the compensation committee of the Company canceled 225,000 shares granted to the CEO in order to conform aggregate issuances to the 675,000 share limitation set forth in the Plan. The Tax Cuts and Jobs Act of 2017 removed the 162(m) qualified performance based compensation exemption to the \$1 million cap on deductions for compensation to covered executives. Section 1.3.2 was in the Plan to permit grants under the Plan to fit within that exemption. As that exemption no longer applies for grants made in 2018 or thereafter, the Plan has been amended to remove the provisions intended to comply with that exemption, including the one in Section 1.3.2. of the Plan. All \$5,328,585 expense has been recorded as a service compensation expense in the year ended March 31, 2018.

Stock options

On November 18, 2014, the Company granted a total of 967,000 shares of stock options under the Plan to a group of a total of 46 grantees including directors, officers and employees. The exercise price of the stock option is \$2.50. The option vests on November 18, 2017, provided that the grantees are still employed by the Company on such a date. The options will be exercisable for five years from the vesting date, or November 18, 2017 until November 17, 2022. For the three months ended December 31, 2018 and 2017, \$0 and \$65,585 was recorded as compensation expense. For the nine months ended December 31, 2018 and 2017, \$0 and \$313,651 was recorded as service compensation expense, respectively. As of December 31, 2018, all compensation costs related to stock option compensation arrangements granted have been recognized.

Statutory reserves

Statutory reserves represent restricted retained earnings. Under Chinese law, the Company is required to set aside 10% of its net income as reported in its statutory accounts into the Statutory Surplus Reserve Fund (the “Reserve Fund”) annually. Once the total amount set aside in the Reserve Fund reaches 50% of the entity’s registered capital, further appropriations become discretionary. The Reserve Fund can be used to increase the entity’s registered capital upon approval by relevant government authorities or eliminate its future losses under PRC GAAP upon a resolution by its board of directors. The Reserve Fund is not distributable to shareholders, as cash dividends or otherwise, except in the event of liquidation.

Appropriations to the Reserve Fund are accounted for as a transfer from unrestricted earnings to statutory reserves. During the three and nine months ended December 31, 2018 and 2017, the Company did not make appropriations to statutory reserves.

There are no legal requirements in the PRC to fund the Reserve Fund by transfer of cash to any restricted accounts, and the Company does not do so.

Note 21 – (LOSS) INCOME PER SHARE

The Company reports earnings per share in accordance with the provisions of the FASB’s related accounting standard. This standard requires presentation of basic and diluted earnings per share in conjunction with the disclosure of the methodology used in computing such earnings per share. Basic earnings per share excludes dilution, but includes vested restricted stocks and is computed by dividing income available to common stockholders by the weighted average common shares outstanding during the period. Diluted earnings per share takes into account the potential dilution that could occur if securities or other contracts to issue common stock were exercised and converted into common stock.

The following is a reconciliation of the basic and diluted (loss) earnings per share computation:

| | Three months ended December 31, | | Nine months ended December 31, | |
|---|------------------------------------|----------------|-----------------------------------|----------------|
| | 2018 | 2017 | 2018 | 2017 |
| Net income attributable to controlling interest | \$(1,678,231) | \$(1,625,829) | \$(3,911,501) | \$(4,213,842) |

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| | | | | |
|---|------------|------------|------------|------------|
| Weighted average shares used in basic computation | 28,936,778 | 25,214,678 | 28,936,778 | 25,214,678 |
| Diluted effect of purchase options and warrants | - | - | - | - |
| Weighted average shares used in diluted computation | 28,936,778 | 25,214,678 | 28,936,778 | 25,214,678 |
| Income per share – Basic: | | | | |
| Net (loss) attributable to controlling interest | \$(0.06) | \$(0.08) | \$(0.14) | \$(0.17) |
| Loss per share – Diluted: | | | | |
| Net (loss) attributable to controlling interest | \$(0.06) | \$(0.08) | \$(0.14) | \$(0.17) |

For the three and nine months ended December 31, 2018, 967,000 shares underlying employee stock options and 600,000 shares underlying outstanding purchase options to an investor, and 72,000 shares underlying outstanding purchase option to an investment placement agent were excluded from the calculation of diluted loss per share as the options were anti-dilutive.

Note 22 – SEGMENTS

The Company operates within four main reportable segments: retail drugstores, online pharmacy, drug wholesale and herb farming. The retail drugstores segment sells prescription and over-the-counter (“OTC”) medicines, TCM, dietary supplements, medical devices, and sundry items to retail customers. The online pharmacy sells OTC drugs, dietary supplements, medical devices and sundry items to customers through several third-party platforms such as Alibaba’s Tmall, JD.com and Amazon.com, and the Company’s own platform all over China. The drug wholesale segment includes supplying the Company’s own retail drugstores with prescription and OTC medicines, TCM, dietary supplement, medical devices and sundry items (which sales have been eliminated as intercompany transactions), and also selling them to other drug vendors and hospitals. The Company’s herb farming segment cultivates selected herbs for sales to other drug vendors. The Company is also involved in online sales and clinic services that do not meet the quantitative thresholds for reportable segments and are included in the retail drugstores segment. The segments’ accounting policies are the same as those described in the summary of significant accounting policies. The Company evaluates performance based on profit or loss from operations before interest and income taxes not including nonrecurring gains and losses.

The Company’s reportable business segments are strategic business units that offer different products and services. Each segment is managed separately because they require different operations and markets to distinct classes of customers.

The following table presents summarized information by segment of the continuing operations for the three months ended December 31, 2018.

| | Retail drugstores | Online Pharmacy | Drug wholesale | Herb farming | Total |
|-------------------------------------|----------------------|--------------------|-------------------|-----------------|--------------|
| Revenue | \$20,867,250 | \$2,493,205 | 7,556,094 | - | 30,916,549 |
| Cost of goods | 14,903,761 | 2,232,994 | 6,644,008 | - | 23,780,763 |
| Gross profit | \$5,963,489 | \$260,211 | 912,086 | - | 7,135,786 |
| Selling expenses | 4,819,081 | 438,235 | 1,431,261 | - | 6,688,577 |
| General and administrative expenses | 1,443,634 | 47,703 | 1,081,525 | - | 2,572,862 |
| Loss income from operations | \$(299,226) | \$(225,727) | (1,600,700) | - | (2,125,653) |
| Depreciation and amortization | \$449,893 | \$- | 433 | - | 450,326 |
| Total capital expenditures | \$6,415,414 | \$- | 314 | - | 6,415,728 |

The following table presents summarized information by segment of the continuing operations for the three months ended December 31, 2017.

| | Retail drugstores | Online Pharmacy | Drug wholesale | Herb farming | Total |
|-------------------------------------|----------------------|--------------------|-------------------|-----------------|--------------|
| Revenue | \$18,288,222 | \$3,395,047 | 5,128,973 | - | 26,812,242 |
| Cost of goods | 13,686,969 | 3,134,767 | 4,418,893 | - | 21,240,629 |
| Gross profit | \$4,601,253 | \$260,280 | 710,080 | - | 5,571,613 |
| Selling expenses | 3,509,018 | 572,397 | 939,556 | - | 5,020,971 |
| General and administrative expenses | 930,689 | 174,865 | 1,615,560 | 16,668 | 2,737,782 |
| Income (Loss) from operations | \$161,546 | \$(486,982) | (1,845,036) | (16,668) | (2,187,140) |
| Depreciation and amortization | \$(525,203) | \$- | 4,649 | - | (520,554) |
| Total capital expenditures | \$8,9495 | \$- | 4,711 | - | 94,206 |

The following table presents summarized information of the continuing operation by segment for the nine months ended December 31, 2018:

| | Retail drugstores | Online pharmacy | Drug wholesale | Herb farming | Total |
|------------------|----------------------|--------------------|-------------------|-----------------|------------|
| Revenue | \$54,971,889 | \$6,637,922 | 19,488,350 | | 81,098,161 |
| Cost of goods | 39,344,927 | 5,883,301 | 17,320,243 | | 62,548,471 |
| Gross profit | \$15,626,962 | \$754,621 | 2,168,107 | | 18,549,690 |
| Selling expenses | 12,453,077 | 1,316,945 | 2,769,056 | | 16,539,078 |

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| | | | | |
|-------------------------------------|----------------|--------------|--------------|--------------|
| General and administrative expenses | 4,644,077 | 292,544 | 1,406,081 | 6,342,874 |
| Loss from operations | \$(1,470,364) | \$(854,868) | (2,007,030) | (4,332,262) |
| Depreciation and amortization | \$980,845 | \$- | 7,446 | 988,291 |
| Total capital expenditures | \$6,789,129 | \$- | 1,437 | 6,790,566 |

The following table presents summarized information of the continuing operation by segment for the nine months ended December 31, 2017:

| | Retail drugstores | Online pharmacy | Drug wholesale | Herb farming | Total |
|-------------------------------------|----------------------|--------------------|-------------------|-----------------|--------------|
| Revenue | \$46,356,207 | \$9,595,752 | 16,021,694 | - | 71,973,653 |
| Cost of goods | 34,227,630 | 8,644,564 | 13,794,588 | - | 56,666,782 |
| Gross profit | \$12,128,577 | \$951,188 | 2,227,106 | - | 15,306,871 |
| Selling expenses | 8,510,663 | 1,547,569 | 3,230,370 | - | 13,288,602 |
| General and administrative expenses | 4,942,902 | 352,770 | 1,996,393 | 26,715 | 7,318,780 |
| Loss income from operations | \$(1,324,988) | \$(949,151) | (2,999,657) | (26,715) | (5,300,511) |
| Depreciation and amortization | \$(854,445) | \$- | 209,023 | - | (645,422) |
| Total capital expenditures | \$295,637 | \$- | 10,927 | - | 306,564 |

The Company does not have long-lived assets located outside the PRC. In accordance with the enterprise-wide disclosure requirements of FASB's accounting standard, the Company's net revenue from external customers through its retail drugstores by main product category is as follows:

| | Three months ended December 31, | | Nine months ended December 31, | |
|-------------------------|------------------------------------|--------------|-----------------------------------|--------------|
| | 2018 | 2017 | 2018 | 2017 |
| Prescription drugs | \$6,756,073 | \$5,373,870 | \$17,835,700 | \$14,860,659 |
| OTC drugs | 9,393,148 | 9,168,708 | 24,018,263 | 21,593,385 |
| Nutritional supplements | 1,869,351 | 1,883,020 | 4,750,013 | 4,558,383 |
| TCM | 1,342,768 | 1,185,004 | 4,615,033 | 3,136,203 |
| Sundry products | 248,729 | 180,338 | 799,554 | 804,817 |
| Medical devices | 1,257,180 | 497,282 | 2,953,326 | 1,402,760 |
| Total | \$20,867,249 | \$18,288,222 | \$54,971,889 | \$46,356,207 |

The Company's net revenue from external customers through online pharmacy by main product category is as follows:

| | Three months ended December 31, | | Nine months ended December 31, | |
|-------------------------|------------------------------------|-----------|-----------------------------------|-----------|
| | 2018 | 2017 | 2018 | 2017 |
| Prescription drugs | \$- | \$- | \$- | \$- |
| OTC drugs | 837,126 | 1,535,383 | 2,412,057 | 4,038,674 |
| Nutritional supplements | 220,776 | 514,952 | 575,862 | 1,365,834 |

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| | | | | |
|-----------------|-------------|-------------|-------------|-------------|
| TCM | 28,785 | 8,802 | 54,417 | 18,984 |
| Sundry products | 573,993 | 224,514 | 2,128,282 | 1,065,935 |
| Medical devices | 832,526 | 1,111,396 | 1,467,304 | 3,106,325 |
| Total | \$2,493,206 | \$3,395,047 | \$6,637,922 | \$9,595,752 |

The Company's net revenue from external customers through wholesale by main product category is as follows:

| | Three months ended | | Nine months ended | |
|-------------------------|----------------------|-------------|----------------------|--------------|
| | December 31, 2018 | 2017 | December 31, 2018 | 2017 |
| Prescription drugs | \$3,933,441 | \$2,777,566 | \$11,708,683 | \$9,252,199 |
| OTC drugs | 3,341,676 | 2,303,726 | 7,246,356 | 6,652,879 |
| Nutritional supplements | 167,069 | 19,123 | 240,666 | 47,660 |
| TCM | 77,216 | 20,876 | 156,525 | 21,480 |
| Sundry products | 5,949 | - | 21,479 | - |
| Medical devices | 30,743 | 7,682 | 114,641 | 47,476 |
| Total | \$7,556,094 | \$5,128,973 | \$19,488,350 | \$16,021,694 |

Note 23 – COMMITMENTS AND CONTINGENCIESOperating lease commitments

The Company recognizes lease expenses on a straight line basis over the term of its leases in accordance with the relevant accounting standards. The Company has entered into various tenancy agreements for its store premises and for the land leased from a local government to farm herbs.

The Company's commitments for minimum rental payments under its leases for the next five years and thereafter are as follows:

| Periods ending September 30, | Retail drugstores | Online pharmacy | Drug wholesale | Herb farming | Total Amount |
|------------------------------|-------------------|-----------------|----------------|--------------|--------------|
| 2019 | \$4,590,468 | \$ - | \$ - | \$ - | \$4,590,468 |
| 2020 | 3,699,758 | - | - | - | 3,699,758 |
| 2021 | 2,799,515 | - | - | - | 2,799,515 |
| 2022 | 2,013,152 | - | - | - | 2,013,152 |
| 2023 | 1,342,827 | - | - | - | 1,342,827 |
| Thereafter | 1,762,033 | - | - | - | 1,762,033 |

Total rent expense amounted to \$1,194,247 and \$1,184,452 for the three months ended December 31, 2018 and 2017, respectively. Total rent expense amounted to \$3,586,552 and \$3,114,851 for the nine months ended December 31, 2018 and 2017, respectively.

Note 24 – Subsequent Events

The Company's management has evaluated subsequent events through the date these financial statements were issued, and there were no material subsequent events requiring adjustments to the financial statements or disclosure.

**ITEM MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS
2. OF OPERATIONS.**

The following management’s discussion and analysis should be read in conjunction with our unaudited condensed consolidated financial statements and the notes thereto and the other financial information appearing elsewhere in this item. In addition to historical information, the following discussion contains certain forward-looking statements within the “safe harbor” provisions of the Private Securities Litigation Reform Act of 1995. These statements relate to our future plans, objectives, expectations and intentions. These statements may be identified by the use of words such as “may,” “will,” “could,” “expect,” “anticipate,” “intend,” “believe,” “estimate,” “plan,” “predict,” and similar terms or terminology, or the negative of such terms or other comparable terminology. Although we believe the expectations expressed in these forward-looking statements are based on reasonable assumptions within the bound of our knowledge of our business, our actual results could differ materially from those discussed in these statements. Factors that could contribute to such differences include, but are not limited to, those discussed in the “Risk Factors” section of our annual report on Form 10-K for the year ended March 31, 2018 and filed with the SEC on June 29, 2018. We undertake no obligation to update publicly any forward-looking statements for any reason even if new information becomes available or other events occur in the future.

Our financial statements are prepared in U.S. Dollars and in accordance with accounting principles generally accepted in the United States. See “Exchange Rates” below for information concerning the exchanges rates at which Renminbi (“RMB”) were translated into U.S. Dollars (“USD” or “\$”) at various pertinent dates and for pertinent periods.

Overview

We currently operate in four business segments in China: (1) retail drugstores, (2) online pharmacy, (3) wholesale of products similar to those that we carry in our pharmacies, and (4) farming and selling herbs used for traditional Chinese medicine (“TCM”).

Our drugstores offer customers a wide variety of pharmaceutical products, including prescription and over-the-counter (“OTC”) drugs, nutritional supplements, TCM, personal and family care products, medical devices, and convenience products, including consumable, seasonal, and promotional items. Additionally, we have licensed doctors of both western medicine and TCM available on site for consultation, examination and treatment of common ailments at scheduled hours. As of December 31, 2018, we had 122 pharmacies in Hangzhou under the store brand of “Jiuzhou Grand Pharmacy.” During the nine months ended December 31, 2018, we relocated eleven of our stores in Hangzhou City.

Since May 2010, we have also been selling certain OTC drugs, medical devices, nutritional supplements and other sundry products online. Our online pharmacy sells through several third-party platforms such as Alibaba's Tmall, JD.com and Amazon.com, and the Company's own platform all over China. Our sales through our own platform are primarily generated by customers who use their private commercial medical insurances package.

We operate a wholesale business through Jiuxin Medicine distributing third-party pharmaceutical products (similar to those carried by our pharmacies) primarily to trading companies throughout China. We also planted ginkgo trees but have not incurred sales in the nine months ended December 31, 2018.

Critical Accounting Policies and Estimates

In preparing our audited consolidated financial statements in accordance with accounting principles generally accepted in the United States of America, we are required to make judgments, estimates and assumptions that affect: (i) the reported amounts of our assets and liabilities; (ii) the disclosure of our contingent assets and liabilities at the end of each reporting period; and (iii) the reported amounts of revenue and expenses during each reporting period. We continually evaluate these estimates based on our own historical experience, knowledge and assessment of current business and other conditions, our expectations regarding the future based on available information and reasonable assumptions, which together form our basis for making judgments about matters that are not readily apparent from other sources. Since the use of estimates is an integral component of the financial reporting process, our actual results could differ materially from those estimates.

We believe that any reasonable deviation from those judgments and estimates would not have a material impact on our financial condition or results of operations. To the extent that the estimates used differ from actual results, however, adjustments to the statement of operations and corresponding balance sheet accounts would be necessary. These adjustments would be made in future financial statements.

When reading our financial statements, you should consider: (i) our critical accounting policies; (ii) the judgment and other uncertainties affecting the application of such policies; and (iii) the sensitivity of reported results to changes in conditions and assumptions. The critical accounting policies and related judgments and estimates used to prepare our financial statements are identified in Note 2 to our audited consolidated financial statements accompanying in this report.

In May 2014, the FASB issued ASU No. 2014-09, which creates Topic 606, Revenue from Contracts with Customers. The new guidance outlines a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers. The core principle of the guidance is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods and services. Additionally, the guidance requires improved disclosure to help users of financial statements better understand the nature, amount, timing, and uncertainty of revenue that is recognized. The new guidance supersedes most current revenue recognition guidance, including industry-specific guidance. The standard is effective for annual reporting periods beginning after December 15, 2017, including interim periods within that reporting period, and permits early adoption on a limited basis. The update permits the use of either the retrospective or cumulative effect transition method. On April 1, 2018, we adopted the guidance in ASC 606 and all the related amendments and applied the new revenue standard to all contracts using the modified retrospective method. Based on the new standard our revenue recognition policies related to membership rewards programs will change. But the impact of the new revenue standard was not material and there was no adjustment required to the opening balance of retained earnings. We expect the impact of the adoption of the new revenue standard to be immaterial to our net income on an ongoing basis.

We currently recorded awarded membership points as accrued expense. The adoption of the policy will require us to deduct the membership rewards directly from our retail revenue. In other words, we will present such amounts in net sales as opposed to our current reduction of operation expense classification.

Results of Operations

Comparison of the three months ended December 31, 2018 and 2017

The following table summarizes our results of operations for the three months ended December 31, 2018 and 2017:

| | Three months ended December 31, 2018 | | 2017 | | | |
|--|---|-----------------------------------|--------|-----------------------------------|-------|----|
| | Amount | Percentage of total revenue | Amount | Percentage of total revenue | | |
| Revenue | \$30,916,549 | 100.0 | % | \$26,812,242 | 100.0 | % |
| Gross profit | \$7,135,786 | 23.1 | % | \$5,571,613 | 20.8 | % |
| Selling expenses | \$6,688,577 | 21.6 | % | \$5,020,971 | 18.7 | % |
| General and administrative expenses | \$2,572,862 | 8.3 | % | \$2,737,782 | 10.2 | |
| Loss from operations | \$(2,125,653) | (6.9 |)% | \$(2,187,140) | (8.2 |)% |
| Interest income | \$18,964 | 0.1 | % | \$76,266 | 0.3 | % |
| Interest expenses | \$- | - | % | \$- | - | % |
| Other income, net | \$32,795 | 0.1 | % | \$301,292 | 1.1 | % |
| Change in fair value of derivative liability | \$(85,115) | (0.3 |)% | \$221,859 | 0.8 | % |
| Income tax expense | \$47,958 | 0.2 | % | \$38,106 | 0.1 | % |
| Net income (loss) | \$(2,206,967) | (7.1 |)% | \$(1,625,829) | (6.1 |)% |

Revenue

Due to the growth in our retail drugstores business and wholesale business, revenue increased by \$4,104,307 or 15.3% for the three months ended December 31, 2018, as compared to the three months ended December 31, 2017, offset by the decrease in our online sales. The following table breaks down the revenue for our four business segments for the three months ended December 31, 2018 and 2017:

Revenue by Segment

The following table breaks down the revenue for our four business segments for the three months ended December 31, 2018 and 2017:

| | For the three months ended December 31, 2018 | | 2017 | | Variance by amount | % of change | |
|---------------------------------|---|-----------------------|----------------|--------------------------|--------------------------|----------------|----|
| | Amount | % of total revenue | Amount | % of total revenue | | | |
| Revenue from retail drugstores | \$20,867,249 | 67.5 | % \$18,288,222 | 68.2 | % \$2,579,027 | 14.1 | % |
| Revenue from online sales | 2,493,206 | 8.1 | % 3,395,047 | 12.7 | % (901,841) | (26.6 |)% |
| Revenue from wholesale business | 7,556,094 | 24.4 | % 5,128,973 | 19.1 | % 2,427,121 | 47.3 | % |
| Revenue from farming business | - | - | % - | - | % - | - | % |
| Total revenue | \$30,916,549 | 100.0 | % \$26,812,242 | 100.0 | % \$4,104,307 | 15.3 | % |

Retail drugstores sales, which accounted for approximately 67.5% of total revenue for the three months ended December 31, 2018, increased by \$2,579,027, or 14.1% compared to the three months ended December 31, 2017, to \$18,288,222. Same-store sales increased by approximately \$1,976,955, or 11.3%, while new stores contributed approximately \$642,527 in revenue in the three months ended December 31, 2018.

The increase in our retail drugstore sales is primarily due to consumer-facing benefits such as emphasis on onsite medical care, chronic disease management services, incremental DTP (Direct-to-Patient) business caused by continuous hospital medical reform, promotional campaigns such as our fifteen year anniversary sales, and maturing of stores opened a year ago. Convenient onsite medical support at our pharmacies has been our hallmark from the beginning of our business. Suitable medical support from our doctors has proven to be critical to our superior store sales. Linking doctor care with drug sales has become our business guidance for the future. By adding more doctor-provided services at stores, we have been able to promote our store sales. In January 2019, we had a grand opening of another flagship store in South Hangzhou. The store hosts both our drugstore and clinic and is expected to expand our business models.

DTP drugs are usually low profit margin new medicines not sold at hospitals. As part of the PRC's recent medical reform package, local governments require the revenue percentage from drug sales at public hospitals to decline year by year. In order to achieve lower drug sales percentage out of their total revenue, the public hospitals chose to abandon sales of low profit margin DTP products first. As the biggest drugstore network in Hangzhou City, quite a few of our stores are located adjacent to local hospitals. Additionally, we have actively contacted local vendors of certain DTP products that we were previously not selling and were able to sell these DTP products in our stores. By opening special counters at some stores and selling more DTP products, sales in our drugstores have increased.

Implementing marketing campaigns suited to local communities has been an important tool in driving sales. We usually cooperated with brand-name pharmaceutical manufacturers in our marketing campaigns. Brand-name medical products sales improve our store reputation, which is beneficial to our long-term sales.

Furthermore, since fiscal year 2018, we have accelerated our expansion of new stores, which is expected to generate more retail drugstore revenues. Eighteen stores have become qualified for municipal government insurance reimbursement after about a year's operation. Sales reimbursed from municipal government insurance program usually account for more than 50% of our total store sales. As these stores gained such qualifications, their sales increased quickly as compared to the previous year. Our store count increased to 122 as of December 31, 2018, compared to 113 stores as of December 31, 2017.

Our online pharmacy sales decreased by approximately \$901,841, or 26.6% for the three months ended December 31, 2018, as compared to the three months ended December 31, 2017. The decrease was primarily caused by a decline in our sales via various e-commerce platforms, offset by the increase in business referred from Pharmacy Benefit

Management (“PBM”) providers, as further explained below, during this three month period. We carry our business either through certain e-commerce platforms such as Tmall and JD.com or via our own official online pharmacy website. Such arrangements with third-party platforms have exposed our online presence to a wider consumer base.

Our official website sales increased by \$32,363 or 6.1% period over period, primarily as we explored more PBM providers, who draw insured from private health insurance companies to spend on health products at drugstores. In order to increase the popularity of our products, we have made considerable efforts to identify popular products that can drive sales, while keeping a close watch on cost. However, due to the official suspension of OTC drug sales on e-commerce platforms such as Alibaba and strong competition, our sales via these e-commerce platforms have been curtailed. As a result, our sales via these e-commerce platforms decreased by 32.6% period over period. We are adding more non-medical health products such as nutritional supplements into our sales menu to counteract the decline in sale of OTC drug category.

Wholesale revenue increased by \$2,427,121 or 47.3%. As our retail drugstores achieved large quantity sales of certain brand name products, we were able to bargain for lower purchase prices than the market level on these merchandises. As a result, vendors who were unable to obtain a better price than ours, turned to us for these products, causing the increase in the wholesale volume. Additionally, we strategically act as provincial agent for Dong’e Ejiao and sold significant amounts of Ejiao with in Zhejiang Province. However, hospitals are still the dominant drug retailers in China. Local hospitals usually have strong ties with their existing suppliers and we have not been able to make significant progress in becoming a major supplier to local hospitals.

In the three months ended December 31, 2018 and 2017, we have not generated revenue from our farming business. We planted ginkgo and maidenhair trees during the year ended June 30, 2013. A ginkgo tree may have a growth period of up to twenty years before it is mature enough to be harvested. We have not yet harvested our ginkgo or maidenhair trees. Usually, the longer it grows the more valuable it becomes. We plan to continue cultivating the trees in order to maximize their market value in the future. We anticipate that we will continue to grow ginkgo trees and start cultivating other herbs in the future.

Gross Profit

Gross profit increased by \$1,564,173 or 28.1% period over period primarily as a result of an increase in revenue from the retail business, which increased significantly in the three months ended December 31, 2018. At the same time, gross margin increased from 20.8% to 23.1% due to higher retail and online profit margins. The average gross margins for each of our four business segments are as follows:

| | For the three months ended December 31, 2018 | | 2017 |
|---|---|--------|------|
| Average gross margin for retail drugstores | 28.6 % | 25.2 % | |
| Average gross margin for online sales | 10.4 % | 7.7 % | |
| Average gross margin for wholesale business | 12.1 % | 13.8 % | |
| Average gross margin for farming business | N/A | N/A | |

Retail gross margins increased primarily because of introducing new suppliers, and regularly renegotiating prices with our suppliers. By hiring talented sales employees, who have decades of experience in the drug sales and purchase industry, we were able to introduce new suppliers and sign brand name product contracts to obtain more rebates. As a result, we were able to keep up with our sale profit margin. In addition, we are able to regularly renegotiate with our vendors and press prices down to an acceptable level, we expect to keep our profit margin at a reasonable level in the future.

Gross margin of online pharmacy sales increased primarily due to the increase in our sales via our own official website, as well as due to decrease in sale via third-party platforms, which are usually subject to low profit margin. We conduct our business either through certain ecommerce platforms such as Tmall and JD.com or via our own official online pharmacy website, www.dada360.com. The sales on our own official website usually have higher profit margins because customers referred by commercial insurance companies are premium customers who can afford premium products with higher profit margins. As described in the above, during the three months ended December 31, 2018, we achieved more sales from our own official websites. As a result, we incurred higher profit margin.

Wholesale gross margin varies period by period primarily as a result of different products we carry and sell to certain pharmaceutical vendors. In the three months ended December 31, 2018, we have acted as the provincial agent for Dong'e Ejiao and distributed a significant amount of Ejiao in Zhejiang Province. Ejiao is a popular product sold as a nutritional supplement in large quantities in the winter months. Dong'e is a reputable brand of Ejiao and has low wholesale profit margin of approximately 8.7%. As we have become its major wholesale distributor in Zhejiang Province in 2018, we purchased and sold a large quantity in October 2018. As a result, our overall wholesale gross profit margin was significantly lowered. Although we have attempted to market our products to major local hospitals

and other pharmacies, we have not been able to make significant progress. Until we are able to obtain status as a provincial or national exclusive sales agent for certain popular drugs or have sales access to large local hospitals, we may have to maintain low profit margins in order to drive sales on our wholesale business.

Selling and Marketing Expenses

Selling and marketing expenses increased by \$1,667,606, or 33.2%, as compared to the same period of the last fiscal year, primarily due to increases in marketing and sales staff expenses and rental expenses related to our store expansion. We opened more than 57 new stores in Hangzhou and ten new stores in Lin'An under Lin'An Jiuzhou. To quickly attract local customers and expand our business, we hired additional in-store staff and arranged various promotional campaigns. The labor costs increased by approximately \$1.2 million. For example, during the three months ended December 31, 2018, the total selling expenses related to Lin'An Jiuzhou was \$205,464 as compared to \$84,771 in the three months ending December 31, 2017. Additionally, labor expense included in Jiuzhou Pharmacy selling expense increased by \$0.3 million. Overall, such expenses as a percentage of our revenue kept at 21.6% and 18.7%, respectively, for the three months ended December 31, 2018 and 2017.

General and Administrative Expenses

General and administrative expenses decreased by \$164,920, or 6.0%, as compared to the same period of last year. Such expenses as a percentage of revenue decreased to 8.3% from 10.2% for the same period a year ago. In the three months ended December 31, 2018, our bad debt expense decreased by \$0.3 million from the same period a year ago. Excluding such an effect, the general and administrative expense increased by approximately \$139,861, which reflects our hiring of additional management talent in our headquarter.

Loss from Operations

As a result of the above, we had loss from operations of \$2,125,653 in the quarter ended December 31, 2018, as compared to loss from operations of \$2,187,140 a year ago. Our operating margin for the three months ended December 31, 2018 and 2017 was (6.9)% and (8.2)%, respectively.

Income Taxes

Our income tax expense decreased by \$9,852 period over period due to a decrease in overall profit.

Net Loss

As a result of the foregoing, net loss is \$2,206,967 in the three months ended December 31, 2018 as compared to a net loss of \$1,625,829 in the three months ended December 31, 2017.

Comparison of nine months ended December 31, 2018 and 2017

The following table summarizes our results of operations for the nine months ended December 31, 2018 and 2017:

| | Nine months ended December 31, 2018 | | 2017 | | | |
|--|--|-----------------------------------|--------|-----------------------------------|-------|----|
| | Amount | Percentage of total revenue | Amount | Percentage of total revenue | | |
| Revenue | \$81,098,161 | 100.0 | % | 71,973,653 | 100.0 | % |
| Gross profit | \$18,549,690 | 22.9 | % | 15,306,871 | 21.3 | % |
| Selling expenses | \$16,539,078 | 20.4 | % | 13,288,602 | 18.5 | % |
| General and administrative expenses | \$6,342,874 | 7.8 | % | 7,318,780 | 10.2 | % |
| Loss from operations | \$(4,332,262) | (5.3 |)% | (5,300,511) | (7.4 |)% |
| Interest income | 92,196 | 0.1 | % | 479,509 | 0.7 | % |
| Other income, net | \$(12,436) | 0.0 | % | 263,241 | 0.4 | % |
| Change in fair value of derivative liability | \$(173,955) | (0.2 |)% | 420,610 | 0.6 | % |
| Income tax expense | \$104,712 | 0.1 | % | 76,691 | 0.1 | % |
| Net loss | \$(4,506,297) | (5.6 |)% | (4,213,842) | 5.9 | % |

Revenue

Primarily due to the increase in our retail pharmacy business and wholesale business, our revenue increased by \$9,124,508 or 12.7% for the nine months ended December 31, 2018, as compared to the nine months ended December 31, 2017, partially offset by the increase in our retail drugstores. The following table breaks down the revenue for our four business segments for the nine months ended December 31, 2018 and 2017.

Quarterly Revenue by Segment

The following table breaks down the revenue for our four business segments for the nine months ended December 31, 2018 and 2017:

| | Nine months ended December 31, 2018 | | 2017 | | Variance by amount | % of change |
|---------------------------------|--|--------------------------|--------------|--------------------------|-----------------------|----------------|
| | Amount | % of total revenue | Amount | % of total revenue | | |
| Revenue from retail drugstores | \$54,971,889 | 67.8 % | \$46,356,207 | 64.4 % | \$8,615,682 | 18.6 % |
| Revenue from online sales | 6,637,922 | 8.2 % | 9,595,752 | 13.3 % | (2,957,830) | (30.8)% |
| Revenue from wholesale business | 19,488,350 | 24.0 % | 16,021,694 | 22.3 % | 3,466,656 | 21.6 % |
| Revenue from farming business | - | - % | - | - % | - | - % |
| Total revenue | \$81,098,161 | 100.0 % | \$71,973,653 | 100.0 % | \$9,124,508 | 12.7 % |

Retail drugstores sales, which accounted for approximately 67.8% of total revenue for the nine months ended December 31, 2018, increased by \$8,615,682, or 18.6% as compared to the nine months ended December 31, 2017, to \$46,356,207. Same-store sales increased by approximately \$6,947,420, or 15.6%, while new stores contributed approximately \$1,409,463 in revenue in the nine months ended December 31, 2018.

The increase in our retail drugstore sales is primarily due to consumer-facing benefits such as emphasis on onsite medical care, chronic disease management, incremental DTP (Direct-to-Patient) business caused by continuous hospital medical reform, and maturing of stores opened a year ago. Convenient onsite medical support at our pharmacies has been our hallmark from the beginning of our business. Suitable medical support from our doctors has proven to be critical to our superior store sales. It is our long-term goal to add more medical care into our store chain and create a new retail drugstore model. By adding more medical service at stores, we have been able to promote our store sales.

As the PRC's medical reform continues, more and more drug prescriptions have flowed out of hospitals. DTP drugs are usually low profit margin new medicines not sold at hospitals. As part of the aforementioned medical reform package, local governments require the revenue percentages from drug sales at public hospitals to decline year by year. In order to achieve lower drug sales as a percentage of their total revenue, the public hospitals chose to abandon sales of low profit margin DTP products first. As the largest drugstore network in Hangzhou City, quite a few of our stores are located adjacently to local hospitals. Additionally, we have actively contacted local vendors of certain DTP products that we did not previously sell and were able to begin selling these DTP products in our stores. By opening special counters at some stores and selling more DTP products, sales in our drugstores increased.

Furthermore, starting in fiscal 2018, we have accelerated our new store expansion, which we expect to generate increased retail drugstore revenues in the future. In fact, Eighteen stores have become qualified for municipal government insurance reimbursement after about a year's operation. Sales reimbursed from municipal government insurance programs usually account for more than 50% of our total store sales. As these stores gained these qualifications, their sales increased quickly as compared to the previous year. Our store count increased to 122 as of December 31, 2018, compared to 113 stores as of December 31, 2017.

Our online pharmacy sales decreased by approximately \$2,957,830, or 30.8% for the nine months ended December 31, 2018, as compared to the nine months ended December 31, 2017. The decrease was primarily caused by declines in our sales via various e-commerce platforms, partially offset by the increase in business referred from Pharmacy Benefit Management ("PBM") providers and, as further explained below, during this nine months. We carry our business either through certain e-commerce platforms such as Tmall and JD.com or via our own official online pharmacy website. Such arrangements with third-party platforms have exposed our online presence to a wider consumer base.

Our official website sales increased by \$266,636 or 20.2% period over period, primarily as we explored more PBM providers, who draw insured from private health insurance company to spend on health products at drugstores. In order to increase the popularity of our products, we have made considerable efforts to identify popular products that can drive sales, while keeping a close watch on cost. However, due to the official suspension of OTC drug sales on e-commerce platforms such as Alibaba and strong competition, our sales via these e-commerce platforms have been curtailed. As a result, our sales via these e-commerce platforms decreased by 39.0% period over period. We are adding more non-medical health products such as nutritional supplements into our sales menu to counteract the decline in sale of OTC drug category.

Wholesale revenue increased by \$3,466,656 or 21.6%, primarily as a result of our ability to resell certain products, which our retail stores made large orders on, to other vendors. As our retail drugstores achieved large quantity sales of certain brand name products, we were able to bargain for lower purchase prices than the market level on such merchandise. As a result, vendors who were unable to obtain a better price than ours, turned to us for these products, causing the wholesale volume to grow. Additionally, we strategically act as provincial agent for Dong'e Ejiao and sold significant amount of Ejiao in September within Zhejiang Province. However, hospitals still act as a major source of drug retailers in China. Local hospitals usually have stronger ties with their existing suppliers and we have not been able to make significant progress in becoming a major supplier to local hospitals.

In the nine months ended December 31, 2018 and 2017, we have not harvested and generated revenue from our farming business. We planted ginkgo and maidenhair trees during the year ended March 31, 2013. A ginkgo tree may have a growth period of up to twenty years before it is mature enough for harvest. Usually, the longer it grows the more valuable it becomes. We plan to continue cultivating the trees in order to maximize their market value in the future. During the nine months ended December 31, 2018, we have been evaluating feasibility of planting other herbs with short period of growth. We anticipate that we will continue to grow ginkgo trees and start cultivating other herbs in the future.

Gross Profit

Gross profit increased by \$3,242,819 or 21.2% period over period primarily as a result of an increase in gross margin of retail drugstores. At the same time, gross margin increased from 21.3% to 22.9% due to higher retail profit margins. The average gross margins for each of our four business segments are as follows:

| | Nine months ended December 31, | |
|---|--------------------------------------|-------|
| | 2018 | 2017 |
| Average gross margin for retail drugstores | 28.4% | 26.2% |
| Average gross margin for online sales | 11.4% | 9.9 % |
| Average gross margin for wholesale business | 11.1% | 13.9% |
| Average gross margin for farming business | N/A | N/A |

Retail gross margins increased primarily because of introducing new suppliers, and our efforts to continually renegotiate prices with our suppliers. By hiring talents, who have decades of experience in the drug sales and purchase industry, we were able to introduce new suppliers and sign brand name products contract to obtain more rebates. As a result, we were able to keep up with our sale profit margin. In addition, we are able to continuously renegotiate with our vendors and press price down to an acceptable level, we expect to keep our profit margin at a reasonable level in the future.

Gross margin of online pharmacy sales increased primarily due to the increase in our sales via our own official website, as well as due to decrease in sale via third-party platforms, which are usually subject to low profit margin. We conduct our business either through certain ecommerce platforms such as Tmall and JD.com or via our own official online pharmacy website, www.dada360.com. The sales on our own official website usually have higher profit margins because customers referred by commercial insurance companies are premium customers who can afford premium products with higher profit margins. As described in the above, during the nine months ended December 31, 2018, we achieved more sales from our own official websites. As a result, we incurred higher profit margin.

Wholesale gross margin increased primarily as a result of different products we carried and sold to certain pharmaceutical vendors. In the nine months ended December 31, 2018, we act as the provincial agent for Dong'e Ejiao and distributed significant amount of Ejiao in September within Zhejiang Province. Ejiao is a popular product sold as a nutritional supplement in large quantity in winter. Dong'e is a reputable brand of Ejiao and has low wholesale profit margin of about 8.7%. As we have become its major wholesale distributor in Zhejiang Province in 2018, we purchased and sold a large quantity in September and October 2018. As a result, our gross profit margin lowered significantly. Although we have attempted to market our products to major local hospitals and other pharmacies, we have not been able to make significant progress. Until we are able to obtain status as a provincial or national exclusive sale agent for certain popular drugs or have sales access to large local hospitals, we may have to maintain low profit margins in order to drive sales on our wholesale business.

Selling and Marketing Expenses

Sales and marketing expenses increased by \$3,250,476 or 24.5% period over period, primarily due to increase in marketing and sales staff expense and rental expense related to our store expansion. We have opened 57 new stores in Hangzhou and ten new stores in Lin'An under Lin'An Jiuzhou. To quickly attract local customers and expand our business, we hired additional in-store staff and arranged various promotion campaigns. The labor cost increased by approximately \$2.1 million. For example, during the nine months ended December 31, 2018, the total selling expense related to Lin'An Jiuzhou was \$539,298 as compared to \$171,269 in the nine months ended December 31, 2017. Additionally, labor expense included in Jiuzhou Pharmacy selling expense increased by \$1.44 million. The rental expense increased by approximately \$1.1 million. Overall, such expenses as a percentage of our revenue kept at 20.4% and 18.5% in the nine months ended December 31, 2018 and 2017.

General and Administrative Expenses

General and administrative expenses decreased by \$975,906 or 13.3% period over period. Such expenses as a percentage of revenue decreased to 7.8% from 10.2% for the same period a year ago. In the nine months ended December 31, 2018, our bad debt expense decreased by approximately \$0.85 million from the same period a year ago.. Excluding such an effect, the general and administrative expense only decreased by \$117,904 or 1.8%.

Loss from Operations

As a result of the above, we had loss from operations of \$4,332,262, as compared to loss from operations of \$5,300,511 a year ago. Our operating margin for the nine months ended December 31, 2018 and 2017 was (5.3)% and (7.4)%, respectively.

Income Taxes

Our income tax expense increased by \$28,021 period over period due to overall increase in operation loss in retail profit.

Net Loss

As a result of the foregoing, net loss decreased by \$292,455 period over period.

Accounts receivable

Accounts receivable, which are unsecured, are stated at the amount we expect to collect. We continuously monitor collections and payments from our customers (our distributors) and maintain a provision for estimated credit losses. To prepare for potential loss in such accounts, we made corresponding reserves.

Our accounts receivable aging was as follows for the periods described below:

| From date of invoice to customer | Retail drugstores | Online Pharmacy | Drug wholesale | Herb farming | Total amount |
|----------------------------------|-------------------|-----------------|----------------|--------------|--------------|
| 1- 3 months | \$7,379,463 | \$6,687 | \$1,781,442 | \$ - | \$9,167,592 |
| 4- 6 months | 582,668 | 319 | 777,673 | - | 1,360,660 |
| 7- 12 months | 482,946 | 175,163 | 566,972 | - | 1,225,081 |
| Over one year | 1,686,826 | 4,865 | 2,044,694 | - | 3,736,385 |
| Allowance for doubtful accounts | (2,016,051) | (75,296) | (2,761,055) | - | (4,852,402) |
| Total accounts receivable | \$8,115,852 | \$111,738 | \$2,409,726 | \$- | \$10,637,316 |

Accounts receivable from our retail business mainly consist of reimbursements from government health insurance bureaus and commercial health insurance programs. In the three months ended December 31, 2018, we wrote off an approximately \$36,077 collectible from provincial and Hangzhou City government insurance, as such amount has been determined by the health insurance bureaus to be unqualified for reimbursement. In addition, as we gained experience in operating online pharmacies with good reputation and have provided online operating and network technical support and consulting services to an online business, which intends to run an online health products shop in Hong Kong in 2016. As a result, we recognized revenue and incurred accounts receivables. As the online business company was not able to make profit from its online shop, it has not paid off its account on time. As a result, we made additional reserve on these aged accounts.

Accounts receivable from our online pharmacy business mainly consist of collectibles from third-party platforms such as Tmall and JD.com where we sell products. Usually the third-party platforms will collect from customers ordering on their platforms and then reimburse us in times ranging from several days to a month after orders are placed.

Accounts receivable from our drug wholesale business and herb farming business consist of receivables from our customers such as pharmaceutical distributors. Our drug wholesale business transitioned away from focusing on sales volume beginning in the second half of fiscal 2013, and it tightened its customer credit policy and strengthened monitoring of uncollected receivables. Furthermore, the new management team expended significant efforts in clearing outstanding balances with certain customers and suppliers.

Subsequent to December 31, 2018 and through January 31, 2019, we collected approximately \$3.5 million in receivables relating to our drugstore business, approximately \$1.1 million in receivables relating to our online pharmacy business, approximately \$1.7 million relating to our wholesale business, and \$0 relating to our herb farming business.

Advances to suppliers

Advances to suppliers are mainly prepayments to secure certain products or services at favorable pricing. The aging of our advances to suppliers is as follows for the periods described below:

| From date of cash prepayment to suppliers | Retail drugstores | Online Pharmacy | Drug wholesale | Herb farming | Total amount |
|---|-------------------|-----------------|----------------|--------------|--------------|
| 1- 3 months | \$53,507 | \$ - | \$1,271,629 | \$ - | \$1,325,136 |
| 4- 6 months | 187,711 | - | 1,641,148 | - | 1,828,859 |
| 7- 12 months | 171,228 | - | 576,121 | - | 747,349 |
| Over one year | 593,130 | - | 2,332,095 | - | 2,925,225 |
| Allowance for doubtful accounts | (680,242) | - | (2,657,317) | - | (3,337,559) |
| Total advances to suppliers | \$325,334 | \$ - | \$3,163,676 | \$- | \$3,489,010 |

Since the acquisition of Jiuxin Medicine, we have gradually transferred almost all logistics services of our retail drugstores to Jiuxin Medicine. Jiuzhou Pharmacy only makes purchases on certain non-medical products. As a result, our retail chain had little advances to suppliers as of December 31, 2018.

Advances to suppliers for our drug wholesale business consist of prepayments to our vendors such as pharmaceutical manufacturers and other distributors. We typically receive products from vendors within three to nine months after making prepayments. We continuously monitor delivery from and payments to our vendors while maintaining provisions for estimated credit losses based upon historical experience and any specific supplier issues such as discontinuation of inventory supplies that we have identified. If we are having difficulty receiving products from a vendor, we take the following steps: cease purchasing products from the vendor, ask for return of our prepayment promptly, and if necessary, take legal action. If all of these steps are unsuccessful, management then determines whether the prepayments should be reserved or written off. To facilitate its initial expansion, Jiuxin Medicine made significant prepayments to certain vendors. Lack of timely supplier account reconciliation caused by several sales staff rotations delayed the monitoring of such accounts. To accommodate potential loss in advances to suppliers, we made reserve for amounts considered to be uncollectible. To control credit risk, we have tightened our customer credit policy and strengthened monitoring of uncollected receivables.

Liquidity and Capital Resources

Our cash flows for the periods indicated are as follows:

| | Nine months ended December 31, | |
|---|-----------------------------------|---------------|
| | 2018 | 2017 |
| Net cash provided by/used in operating activities | \$(10,322,880) | \$(9,801,402) |
| Net cash provided by/used in investing activities | \$(6,847,285) | \$(1,756,990) |
| Net cash provided by/used in financing activities | \$7,979,491 | \$5,572,249 |

For the nine months ended December 31, 2018, cash used in operating activities amounted to \$(10,322,880), as compared to \$(9,801,402) a year ago. The change is primarily attributable to a decrease in cash provided by customer deposits of \$2,645,660, a decrease in cash provided by accounts payable of \$4,799,578 offset by an increase of \$943,694 in other payables and accrued liabilities, an increase in inventories and biological assets of \$4,774,158, and an increase in cash provided by the long term deposit of \$1,364,034.

For the nine months ended December 31, 2018, net cash used in investing activities amounted to \$(6,847,285), as compared to \$(1,756,990) used in investing activities a year ago. The change is primarily attributable to purchase of Yueming shop for approximately \$4,722,193 in the nine months ended December 31, 2018.

For the nine months ended December 31, 2018, net cash provided by financing activities amounted to \$7,979,491, as compared to \$5,572,249 net cash used in financing activities a year ago. The increase is primarily due to proceeds from notes payable, offset by decrease repayment of notes payable.

As of December 31, 2018, we had cash and cash equivalents and restricted cash of approximately \$ 20,607,529. Our total current assets as of December 31, 2018, were \$50,876,895 and total current liabilities were \$53,320,838, which resulted in a working capital of \$(2,443,944).

In order to increase our competitive advantages and gain increased local retail pharmacy market share, during fiscal year 2018, we opened 57 new stores in Hangzhou. Additionally, in November 2018, we purchased Yueming shop, a large flagship shop in South Hangzhou. As a result, we incurred significant expenses related to rent, labor hiring and training, and marketing activities. As the retail pharmaceutical market becomes more competitive in recent years, a new store usually cannot make a profit in its first year of operation. In fact, we incurred significant expense with limited incremental revenue in the period we opened new stores.

At their openings, except for four stores, all of the new stores did not have government insurance reimbursement certificates. In fact, it usually takes more than one year for a new store to apply for and obtain the local government insurance reimbursement certificate. We have applied for and received certificates in 2 stores in January 2018 and 11 new stores in June 2018. Historically, sales reimbursed from the government insurance agency accounts for more than half of the total revenue in a mature store. We are actively in the process of applying for certificates for all of our new stores. As more and more new stores obtain certificates, we expect our new store revenue will increase and eventually contribute positive operating cash flow.

In order to increase our ability to serve our customers, we also invested in Linjia Medical, which runs nine clinics adjacent to our drugstores. By introducing a western family doctor system and focusing on pediatrics, we expect our

new clinics to integrate into local communities and eventually contribute positive cash flows to neighborhood Jiuzhou Pharmacy.

On January 23, 2017, we completed a private placement with a single healthcare-focused institutional investor for the purchase of an aggregate of 4,840,000 shares of our common stock at a price of \$2.20 per share and gross proceeds of approximately \$10,648,000. As of December 31, 2018, we had approximately \$1.52 million in our credit line available for further borrowing. We believe that the foregoing sources will collectively meet our liquidity and capital obligations for the next twelve months. However, if we are to acquire additional businesses or further expand our operations, we may need additional capital.

Contractual Obligations and Off-Balance Sheet Arrangements

Contractual Obligations

When we open store locations, we typically enter into lease agreements that are generally between three to ten years. Our commitments for minimum rental payments under our leases for the next five years and thereafter are as follows:

| Periods ending September 30, | Retail drugstores | Online pharmacy | Drug wholesale | Herb farming | Total Amount |
|------------------------------|----------------------|--------------------|-------------------|-----------------|-----------------|
| 2019 | \$4,590,468 | \$ - | \$ - | \$ - | \$4,590,468 |
| 2020 | 3,699,758 | - | - | - | 3,699,758 |
| 2021 | 2,799,515 | - | - | - | 2,799,515 |
| 2022 | 2,013,152 | - | - | - | 2,013,152 |
| 2023 | 1,342,827 | - | - | - | 1,342,827 |
| Thereafter | 1,762,033 | - | - | - | 1,762,033 |

Off-balance Sheet Arrangements

We do not have any outstanding financial guarantees or commitments to guarantee the payment obligations of any third parties. We have not entered into any derivative contracts that are indexed to our shares and classified as stockholder's equity or that are not reflected in our consolidated financial statements. Furthermore, we do not have any retained or contingent interest in assets transferred to an unconsolidated entity that serves as credit, liquidity or market risk support to such entity. We do not have any variable interest in any unconsolidated entity that provides financing, liquidity, market risk or credit support to us or engages in leasing, hedging or research and development services with us.

Exchange Rates

Our subsidiaries and affiliated companies in the PRC maintain their books and records in RMB, the lawful currency of the PRC. In general, for consolidation purposes, we translate their assets and liabilities into USD using the applicable exchange rates prevailing at the balance sheet date, and the statement of income is translated at average exchange rates during the reporting period. Adjustments resulting from the translation of their financial statements are recorded as accumulated other comprehensive income.

The exchange rates used to translate amounts in RMB into USD for the purposes of preparing the audited consolidated financial statements or otherwise disclosed in this report were as follows:

| | December 31, 2018 | | March 31, 2018 | |
|--|----------------------|--------|-------------------|--------|
| Balance sheet items, except for the registered and paid-up capital, as of end of period | USD1: RMB | 0.1454 | USD1: RMB | 0.1592 |
| Amounts included in the statement of Operations and statement of cash flows for the period ended | USD1: RMB | 0.1494 | USD1: RMB | 0.1510 |

Inflation

We believe that inflation has not had a material effect on our operations to date.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.

Not applicable.

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ITEM 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

As of December 31, 2018, under the supervision and with the participation of our management team, including our chief executive officer and chief financial officer, we evaluated the effectiveness of the design and operation of our disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended. Based upon this evaluation, our chief executive officer and chief financial officer concluded that, as of the end of the period covered by this report, our disclosure controls and procedures were ineffective at the reasonable assurance level. Such conclusion is based on the presence of the following material weakness in internal control over financial reporting as described in our annual report on Form 10-K for the year ended March 31, 2018:

Accounting and Finance Personnel Weakness - As noted in Item 9A of our annual reports on Form 10-K for the preceding fiscal years, management concluded that in light of the inexperience of our accounting staff with respect to the requirements of U.S. GAAP-based reporting and SEC rules and regulations, we did not maintain effective controls and did not implement adequate and proper supervisory review to ensure that significant internal control deficiencies can be detected or prevented.

Management's assessment of the control deficiency over accounting and finance personnel as of December 31, 2018 considered the same factors, including:

the number of adjustments proposed by our independent auditors during our quarterly review and annual audit processes;

how adequately we complied with U.S. GAAP on transactions; and

how accurately we prepared supporting information to provide to our independent auditors on a quarterly and annual basis.

Based on the above factors, management concluded that the control deficiency over accounting and finance personnel continues to be a material weakness as of December 31, 2018, as our accounting staff continues to lack sufficient U.S. GAAP experience and requires substantial additional training. Specifically, to address the material weakness related to insufficient accounting resources and process necessary to comply with reporting and compliance requirements of the FASB and SEC, we have added personnel who have FASB and SEC reporting and compliance knowledge and experience to the Company and requested advice from outside accounting consultants.

We have been continually making progress in improving internal controls. In 2018, we have successfully completed the installation of a leading ERP system, SAP, from Germany. SAP is a well-known management system used by many Fortune 500 companies. Per the contract with the local SAP system provider, the total fee for SAP customized installation and training adds up to more than one million USD in this year. By automatically connecting commodity flow data with accounting recording, the system minimizes the manual errors made by accounting staff. Additionally, the system provides a view of overall and instant cash information by electronically linking local banking systems with SAP. Additional benefits include automatically-generated customized monthly company performance reports, instant inventory monitoring and reporting, and punctual customer and suppliers accounts maintenance. In later 2018, we have introduced a SAP FICO manager and been optimizing various operation procedures to better fit with the system. We expect to continually improve our internal control system. As such, we will continue our efforts during the fiscal year ending March 31, 2019, although there can be no assurance that compliance will be achieved in this time frame.

Changes in Internal Control over Financial Reporting

There were no changes in our internal control over financial reporting (as defined in Rule 13a-15(f) of the Securities Exchange Act of 1934) during the period covered by this Quarterly Report on Form 10-Q that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II – OTHER INFORMATION

ITEM 6. EXHIBITS.

EXHIBIT INDEX

| Exhibit Number | Description |
|-----------------------|---|
| 10.1 | <u>Amendment No. 5 to 2010 Equity Incentive Plan</u> |
| 10.2 | <u>Offer Letter to Mr. Wei Hu, Chief Operating Officer, dated November 7, 2018 ⁽¹⁾</u> |
| 10.3 | <u>Offer Letter to Ms. Pingfan Wu, an independent director, dated October 26, 2018 ⁽²⁾</u> |
| 31.1 | <u>Section 302 Certification by the Corporation's Chief Executive Officer</u> |
| 31.2 | <u>Section 302 Certification by the Corporation's Chief Financial Officer</u> |
| 32.1 | <u>Section 906 Certification by the Corporation's Chief Executive Officer and Chief Financial Officer</u> |
| 101.INS | XBRL Instance Document |
| 101.SCH | XBRL Taxonomy Extension Schema Document |
| 101.CAL | XBRL Taxonomy Extension Calculation Linkbase Document |
| 101.DEF | XBRL Taxonomy Extension Definition Linkbase Document |
| 101.LAB | XBRL Taxonomy Extension Label Linkbase Document |
| 101.PRE | XBRL Taxonomy Extension Presentation Linkbase Document |

(1) Incorporate by reference from Exhibit 10.1 to the current report on Form 8-K filed by the Company with the SEC on November 9, 2018

(2) Incorporate by reference from Exhibit 10.1 to the current report on Form 8-K filed by the Company with the SEC on October 26, 2018.

SIGNATURES

Pursuant to the requirements 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 JO-JO DRUGSTORES,
INC.**
(Registrant)

Date: February 14, 2019 By: /s/ Lei Liu
Lei Liu
Chief Executive Officer
(Principal Executive Officer)

Date: February 14, 2019 By: /s/ Ming Zhao
Ming Zhao
Chief Financial Officer
(Principal Financial Officer and
Principal Accounting Officer)