

CHINA JO-JO DRUGSTORES, INC.
Form 10-Q
August 15, 2011

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

(Mark One)

☒ Quarterly Report Pursuant To Section 13 Or 15(d) Of The Securities
Exchange Act Of 1934

For the quarterly period ended: June 30, 2011

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
(State or other jurisdiction of incorporation of
origination)

98-0557852
(I.R.S. Employer
Identification Number)

Room 507-513, 5th Floor A Building, Meidu Plaza
Gongshu District, Hangzhou, Zhejiang Province
People's Republic of China
(Address of principal executive offices)

N/A
(Zip code)

+86 (571) 88077078
(Registrant's telephone number, including area code)

(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

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(§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes[X] No []

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

Large accelerated filer [] Accelerated filer []

Non-accelerated filer [] Smaller reporting company [X]

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

APPLICABLE ONLY TO CORPORATE ISSUERS:

Indicate the number of shares outstanding of each issuer's classes of common stock, as of the latest practicable date: 13,571,579 shares issued and outstanding as of August 5, 2011.

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CAUTION REGARDING FORWARD-LOOKING INFORMATION

All statements contained in this Quarterly Report on Form 10-Q ("Form 10-Q") for China Jo-Jo Drugstores, Inc., 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

CONSOLIDATED BALANCE SHEETS

(UNAUDITED)

ASSETS

| | JUNE 30, 2011 | MARCH 31, 2011 |
|------------------------------------|------------------|-------------------|
| CURRENT ASSETS | | |
| Cash | \$ 6,448,109 | \$ 6,489,905 |
| Restricted cash | 683,944 | 921,876 |
| Trade accounts receivable, net | 1,890,080 | 1,484,850 |
| Inventories | 3,672,041 | 4,617,420 |
| Other receivables | 1,196,617 | 1,049,564 |
| Advances to suppliers | 14,786,933 | 16,528,772 |
| Other current assets | 4,573,773 | 8,364,267 |
| Total current assets | 33,251,497 | 39,456,654 |
| PROPERTY AND EQUIPMENT, net | | |
| | 8,862,837 | 5,471,432 |
| OTHER ASSETS: | | |
| Long term deposit | 2,728,661 | 2,540,758 |
| Prepaid - noncurrent | 10,841,016 | 6,075,478 |
| Intangible assets | 357,745 | 390,302 |
| Total other assets | 13,927,422 | 9,006,538 |
| Total assets | \$ 56,041,756 | \$ 53,934,624 |

LIABILITIES AND SHAREHOLDERS' EQUITY

CURRENT LIABILITIES

| | | |
|--------------------------------------|--------------|--------------|
| Accounts payable, trade | \$ 4,129,629 | \$ 3,530,204 |
| Notes payable | 2,273,530 | 2,704,680 |
| Other payables | 319,608 | 627,734 |
| Other payables - related parties | 880,058 | 880,058 |
| Customer deposits | 567,287 | 2,038,608 |
| Taxes payable | 1,653,637 | 1,624,558 |
| Accrued liabilities | 218,144 | 311,639 |
| Total current liabilities | 10,041,893 | 11,717,481 |
| Purchase option derivative liability | 90,594 | 153,226 |
| Total liabilities | 10,132,487 | 11,870,707 |

COMMITMENTS AND CONTINGENCIES

SHAREHOLDERS' EQUITY

Preferred stock; \$0.001 par value; 10,000,000 shares authorized;
nil issued and outstanding as of June 30, 2011 and March 31, 2011

Common stock; \$0.001 par value; 250,000,000 shares authorized;
13,538,747 and 13,530,477 shares issued and outstanding
as of June 30, 2011 and March 31, 2011, respectively

| | | |
|--|---------------|---------------|
| | 13,538 | 13,530 |
| Paid-in capital | 16,362,006 | 16,333,956 |
| Statutory reserves | 1,309,109 | 1,309,109 |
| Retained earnings | 26,530,203 | 23,287,474 |
| Accumulated other comprehensive income | 1,694,413 | 1,119,848 |
| Total shareholders' equity | 45,909,269 | 42,063,917 |
| Total liabilities and shareholders' equity | \$ 56,041,756 | \$ 53,934,624 |

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

CHINA JO-JO DRUGSTORES, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF INCOME AND OTHER COMPREHENSIVE INCOME
(UNAUDITED)

| | Three months ended June 30, | |
|--|-----------------------------|---------------|
| | 2011 | 2010 |
| REVENUES, NET | \$ 21,427,859 | \$ 15,207,428 |
| COST OF GOODS SOLD | 14,558,536 | 10,593,532 |
| GROSS PROFIT | 6,869,323 | 4,613,896 |
| SELLING EXPENSES | 1,378,300 | 823,358 |
| GENERAL AND ADMINISTRATIVE EXPENSES | 1,074,783 | 773,762 |
| OPERATING EXPENSES | 2,453,083 | 1,597,120 |
| INCOME FROM OPERATIONS | 4,416,240 | 3,016,776 |
| OTHER INCOME (EXPENSE), NET | 19,420 | (57,532) |
| CHANGE IN FAIR VALUE OF PURCHASE OPTION DERIVATIVE LIABILITY | 62,632 | 57,944 |
| INCOME BEFORE INCOME TAXES | 4,498,292 | 3,017,188 |
| PROVISION FOR INCOME TAXES | 1,255,563 | 864,724 |
| NET INCOME | 3,242,729 | 2,152,464 |
| OTHER COMPREHENSIVE INCOME | | |
| Foreign currency translation adjustments | 574,565 | 99,422 |
| COMPREHENSIVE INCOME | \$ 3,817,294 | \$ 2,251,886 |
| BASIC AND DILUTED WEIGHTED AVERAGE NUMBER OF SHARES | 13,532,240 | 12,653,848 |
| BASIC AND DILUTED EARNING PER SHARE | \$ 0.24 | \$ 0.17 |

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

CHINA JO-JO DRUGSTORES, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY
(UNAUDITED)

| | Common Stock | | Paid-in capital | Retained Earnings | | Accumulated other comprehensive income (loss) | Total |
|---|---------------------|-----------|--------------------|-----------------------|---------------|---|---------------|
| | Number of shares | Amount | | Statutory reserves | Unrestricted | | |
| BALANCE, March 31, 2010 | 10,000,000 | \$ 10,000 | \$ 877,884 | \$ 1,309,109 | \$ 14,855,016 | \$ (362,260) | \$ 16,689,749 |
| Issuance of common stock | 3,500,000 | 3,500 | 15,705,108 | | | | 15,705,108 |
| Fractional shares due to the one-for-two reverse split | 2 | | | | | | - |
| Reclassification of purchase option to derivative liabilities | | | (402,451) | | | | (402,451) |
| Net Income | | | | | 2,152,464 | | 2,152,464 |
| Foreign currency translation adjustments | | | | | | 99,422 | 99,422 |
| BALANCE, June 30, 2010 | 13,500,002 | \$ 13,500 | \$ 16,180,541 | \$ 1,309,109 | \$ 17,007,480 | \$ (262,838) | \$ 34,247,792 |
| Stock based compensation | 30,745 | 30 | 153,415 | | | | 153,445 |
| Net income | | | | | 6,279,994 | | 6,279,994 |
| Foreign currency translation adjustments | | | | | | 1,382,686 | 1,382,686 |
| BALANCE, March 31, 2011 | 13,530,477 | \$ 13,530 | \$ 16,333,956 | \$ 1,309,109 | \$ 23,287,474 | \$ 1,119,848 | \$ 42,063,917 |
| Stock based compensation | 8,270 | 8 | 28,050 | | | | 28,058 |
| Net income | | | | | 3,242,729 | | 3,242,729 |
| Foreign currency translation adjustments | | | | | | 574,565 | 574,565 |

| | | | | | | | | |
|---------------|------------|-----------|---------------|--------------|---------------|--------------|---------------|--|
| BALANCE, | | | | | | | | |
| June 30, 2011 | 13,538,747 | \$ 13,538 | \$ 16,362,006 | \$ 1,309,109 | \$ 26,530,203 | \$ 1,694,413 | \$ 45,909,269 | |

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

CHINA JO-JO DRUGSTORES, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS
(UNAUDITED)

| | Three months ended June 30, | |
|---|-----------------------------|--------------|
| | 2011 | 2010 |
| CASH FLOWS FROM OPERATING ACTIVITIES: | | |
| Net income | \$ 3,242,729 | \$ 2,152,464 |
| Adjustments to reconcile net income to net cash provided by (used in) operating activities: | | |
| Depreciation and amortization | 262,181 | 148,584 |
| Stock compensation | 28,058 | 40,529 |
| Write off of receivables | 54,691 | - |
| Change in fair value of purchase option derivative liability | (62,632) | (57,944) |
| Change in operating assets: | | |
| Accounts receivable, trade | (438,521) | (211,953) |
| Inventories | 1,000,520 | (177,259) |
| Other receivables | (132,648) | 36,600 |
| Advances to suppliers | 1,947,720 | (3,288,775) |
| Other current assets | 3,879,255 | (256,265) |
| Long term deposit | (153,900) | - |
| Prepaid - noncurrent | 84,061 | (16,938) |
| Change in operating liabilities: | | |
| Accounts payable, trade | 2,093,048 | 1,841,786 |
| Other payables and accrued liabilities | (409,861) | (177,592) |
| Customer deposits | (1,490,217) | - |
| Taxes payable | 7,809 | (99,041) |
| Net cash provided by (used in) operating activities | 9,912,293 | (65,804) |
| CASH FLOWS FROM INVESTING ACTIVITIES: | | |
| Purchase of equipment | (37,760) | (127,334) |
| Additions to leasehold improvements | (955,566) | (315,375) |
| Payments on construction-in-progress | (2,534,126) | - |
| Deposit made to secure business acquisition | (4,745,968) | - |
| Net cash used in investing activities | (8,273,420) | (442,709) |
| CASH FLOWS FROM FINANCING ACTIVITIES: | | |
| Change in restricted cash | 248,687 | (57,958) |
| Payments on notes payable | (2,006,702) | (720,963) |
| Proceeds from equity financing | - | 15,708,608 |
| Proceeds from short-term loans | - | 586,920 |
| Payments on other payables- related parties | - | (54,942) |
| Net cash (used in) provided by financing activities | (1,758,015) | 15,461,665 |
| EFFECT OF EXCHANGE RATE ON CASH | 77,346 | 19,952 |
| (DECREASE) INCREASE IN CASH | (41,796) | 14,973,104 |

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| | | |
|---------------------------|--------------|---------------|
| CASH, beginning of Period | 6,489,905 | 801,593 |
| CASH, end of Period | \$ 6,448,109 | \$ 15,774,697 |

SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:

| | | |
|---|--------------|------------|
| Cash paid for interest | \$ - | \$ 17,352 |
| Cash paid for income taxes | \$ 1,157,526 | \$ 837,658 |
| Non-cash financing activities | | |
| Notes payable transferred to accounts payable vendors | \$ 1,542,619 | \$ 837,307 |

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

CHINA JO-JO DRUGSTORES, INC. AND SUBSIDIARIES

CONDENSED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

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”), where by 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) is, 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”) and Zhejiang Shouantang Medical Technology Co., Ltd. (“Shouantang Technology”), its wholly-owned subsidiaries.

The Company is primarily in the retail drugstore business in the People’s Republic of China (“China” or the “PRC”). As of June 30, 2011, all of the Company’s pharmacies except one were operated by Hangzhou Jiuzhou Grand Pharmacy Chain Co., Ltd. (“Jiuzhou Pharmacy”), a company which the Company controls through contractual arrangements, and Jiuzhou Pharmacy’s wholly-owned subsidiary Shanghai Lydia Grand Pharmacy Co., Ltd. (“Shanghai Lydia”). One drugstore is operated by Hangzhou Quannuo Grand Pharmacy Co., Ltd. (“Hangzhou Quannuo”), a wholly-owned subsidiary of Zhejiang Quannuo Internet Technology Co., Ltd. (“Quannuo Technology”), which is wholly-owned by Shouantang Technology.

The Company also operates two 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. In addition, Hangzhou Jiuxin Qianhong Agriculture Development Co., Ltd. (“Jiuxin Qianhong”), which is wholly-owned by Jiuxin Management, is operating a cultivation project of herbal plants used for traditional Chinese medicine (“TCM”), and Tonglu Lydia Agriculture Development Co., Ltd. (“Tonglu Lydia”), which is wholly-owned by Shouantang Technology, will do the same in the future.

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

| Subsidiaries | Background | Ownership |
|-----------------------|--|-----------|
| Renovation HK | 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 \$4,500,000 fully paid | 100% |
| Shouantang Technology | Established in the PRC on July 16, 2010 by Renovation with registered capital of \$20 million Deemed a WFOE under PRC law \$11 million of registered capital paid as of March 31, 2011, the balance of \$9 million due by July 16, 2012 To carry out internet pharmacy business, is cooperating with the Company’s online store in China to develop its business | 100% |
| Jiuxin Qianhong | Established in the PRC on August 10, 2010 by Jiuxin Management Registered capital of RMB 10,000,000 Renminbi (“RMB”) fully paid To carry out cultivation of TCM herbal plants | 100% |
| Quannuo Technology | Established in the PRC on July 7, 2009 Registered capital of RMB 10,000,000. RMB 2,000,000 was paid and the balance of RMB 8,000,000 was due by July 7, 2011, which is extended with no definite deadline based on local SAIC approval Acquired by Shouantang Technology in November 2010 To develop software for internet pharmacy business, which is cooperating with the Company’s online store in China to develop its business | 100% |
| Hangzhou Quannuo | Established in the PRC on July 8, 2010 by Quannuo Technology Registered capital of RMB 800,000 fully paid Operates one “Quannuo Grand Pharmacy” as a Jiuzhou Pharmacy franchise store in Hangzhou | 100% |
| Tonglu Lydia | Established in PRC on June 24, 2011 by Shouantang Technology Registered capital of RMB 5,000,000 fully paid | 100% |

| | To carry out cultivation of TCM herbal plants | |
|----------------------|---|--|
| Jiuzhou Pharmacy (1) | Established in the PRC on September 9, 2003 Registered capital of RMB 5 million fully paid Operates the “Hangzhou Jiuzhou Grand Pharmacy” stores in and around Hangzhou | VIE by contractual arrangements (2) |
| Jiuzhou Clinic (1) | Established in the PRC as a general partnership on October 10, 2003 Operates a medical clinic adjacent to one of Jiuzhou Pharmacy’s stores | VIE by contractual arrangements (2) |
| Jiuzhou Service (1) | Established in the PRC on November 2, 2005 Registered capital of RMB 500,000 fully paid Operates a medical clinic adjacent to one of Jiuzhou Pharmacy’s stores | VIE by contractual arrangements (2) |
| Shanghai Lydia | Established in the PRC on January 31, 2011 by Jiuzhou Pharmacy Registered capital of RMB 1,000,000 fully paid Operates the “Lydia Grand Pharmacy” store in Shanghai | VIE by contractual arrangements (2) as a wholly-owned subsidiary of Jiuzhou Pharmacy |

(1) Jiuzhou Pharmacy, Jiuzhou Clinic and Jiuzhou Service have been under the common control of the same three owners (the “Owners”) since their respective establishment dates, pursuant to agreements amongst the Owners to vote their interests in concert as memorialized in a voting agreement. Based on such voting agreement, the Company has determined that common control exists among these three companies in accordance with generally accepted accounting standards. Operationally, the Owners have operated these three companies in conjunction with one another since each company’s respective establishment date. Shanghai Lydia is also deemed under the common control of the Owners as it is wholly-owned by 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: consulting services agreement, operating agreement, equity pledge agreement, voting rights agreement and option agreement. As a result of these agreements, which 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 all three companies (as well as the subsidiary 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 Shanghai Lydia, are consolidated into the financial statements of the Company.

Note 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of presentation and consolidation

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with the rules and regulations of the Securities and Exchange Commission (“SEC”) for interim financial statements. Accordingly, they do not include all of the information and footnotes required by U.S. generally accepted accounting principles for complete financial statements. In the opinion of the management, all adjustments (consisting only of normal recurring adjustments) considered necessary for a fair presentation have been included. These condensed consolidated financial statements and notes should be read in conjunction with the audited consolidated March 31, 2011 financial statements and footnotes included in the Company’s annual report on Form 10-K filed with the SEC on June 29, 2011. Operating results for the three months ended June 30, 2011 may not be necessarily indicative of the results that may be expected for the full year.

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, 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, and enable the Company, through Jiuxin Management, to receive a majority of their expected residual returns. The Company has also concluded that Shanghai Lydia is a VIE by virtue of being a wholly-owned subsidiary of Jiuzhou Pharmacy.

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 is 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 the Voting Rights Proxy 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.

Although the Company has determined that the accounting standards regarding consolidation of VIEs do not provide for retroactive accounting treatment, Jiuzhou Pharmacy, Jiuzhou Clinic and Jiuzhou Service in substance were controlled by the Owners on September 9, 2003, October 10, 2003, and November 2, 2005, the establishment dates of

Jiuzhou Pharmacy, Jiuzhou Clinic and Jiuzhou Service, respectively. Such common control conditions resulted in the share exchange transaction to be a capital transaction in substance, reflected as a recapitalization, and the Company has accordingly recorded the consolidation of Renovation at its historical cost.

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, and by changes in governmental policies or interpretations with respect to laws and regulations, anti-inflationary measures, currency conversion, remittances abroad, and rates and methods of taxation, among other things. Although the Company has not experienced losses from these situations and believes that they are in compliance with existing laws and regulations including the 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 which 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 vendors.

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 could 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 consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the 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 consolidated financial statements relate to the assessment of the carrying values of accounts receivable and related allowance for doubtful accounts, useful lives of property and equipment, and fair value of 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 values of financial instruments

The accounting standards regarding fair value of financial instruments and related fair value measurements define fair value, establish a three-level valuation hierarchy for disclosures of fair value measurement and enhance disclosure requirements for fair value measures. The carrying amounts reported in the accompanying consolidated balance sheets for receivables, payables, notes payable and short-term loans qualify as financial instruments and are a reasonable estimate of fair values because of the short period of time between the origination of such instruments and their expected realization and their current market rate of interest. The three levels of valuation hierarchy are defined as follows:

Level 1 inputs to the valuation methodology are quoted prices (unadjusted) for identical assets or liabilities in active markets.

Level 2 inputs to the valuation methodology include quoted prices for similar assets and liabilities in active markets, and inputs that are observable for the assets or liability, either directly or indirectly, for substantially the full term of the financial instruments.

Level 3 inputs to the valuation methodology are unobservable and significant to the fair value.

Revenue recognition

Revenue from sales of prescription medicine at the 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 the drugstores is recognized at the point of sale, which is when the customer pays for and receives the merchandise.

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

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 de minimis.

The Company's revenue is net of value added tax ("VAT") collected on behalf of PRC tax authorities in respect of the sale 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.

Cash and cash equivalents

Cash and cash equivalents include cash on hand, cash on deposit with banks and credit and debit card sales transactions which settle within seven days of the fiscal year-end. The Company considers all highly liquid investments with a maturity of three months or less when purchased to be cash equivalents.

Restricted cash

The Company's restricted cash consists of cash 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 represent amounts due from banks relating to retail sales that are paid or settled by the customers' debit or credit cards, amounts due from government social security bureaus relating to retail sales of drugs, prescription medicine, and medical services that are paid or settled by the customers' medical insurance cards, and 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 needed. The Company uses the aging method to estimate the allowance for anticipated uncollectible receivable balances. Under the aging method, bad debt percentages determined by management, based on historical experience and 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. The ultimate collection of the Company's accounts receivable may take one year. Delinquent account balances are reserved after management determines that the likelihood of collection is not probable, and known bad debts are written-off against allowance for doubtful accounts when identified. For the three months ended June 30, 2011 and 2010, \$54,691 and \$0 accounts receivable were written off.

Inventories

Inventories are stated at the lower of cost or market. Cost is determined using the first in first out method (“FIFO”). Market 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 to ensure that the amounts reflected in the consolidated financial statements at each reporting period are properly stated and valued. The Company records write-downs to inventories for shrinkage losses and damaged merchandise that are identified during the inventory counts. Historically, these amounts have not been material to the consolidated financial statements.

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 following 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 | 3-5 years |
| Motor vehicles | 5 years |
| Office equipment & furniture | 3-5 years |

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

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 asset’s 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. No indication of impairment was noted as of June 30, 2011.

Notes payable

During the normal course of business, the Company constantly issues Bank Acceptance Bills as a payment method to settle down outstanding accounts payables to various material suppliers. The Company recorded such Bank Acceptance Bills as notes payables. The notes payable are generally short term in nature due to their short maturity period of six to nine months.

Income taxes

The Company records income taxes pursuant to the accounting standards for income taxes. These standards require the recognition of deferred income tax liabilities and assets for the expected future tax consequences of temporary differences between income tax basis and financial reporting basis of assets and liabilities. Provision for income taxes consists of taxes currently due and the net change in deferred taxes. A valuation allowance is recognized if it is more likely than not that some portion, or all of, a deferred tax asset will not be realized. As of June 30, 2011 and March 31, 2011, the Company did not have any net deferred tax assets or liabilities.

The FASB's accounting standards clarify the accounting and disclosure 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. Under these standards, a tax position is recognized as a benefit only if it is "more likely than not" that the tax position would be sustained in a tax examination, with a tax examination being presumed to occur. Penalties or interest incurred relating to underpayment of income taxes are classified as income tax expense in the period incurred. No significant penalties or interest relating to income taxes were incurred during the three months ended June 30, 2011 and 2010.

All of the tax returns of the Company, since inception, are subject to examination by the tax authorities.

Value added tax

Sales revenue represents the invoiced value of goods, net of value added tax ("VAT"). All of the Company's products are sold in the PRC and are subject to a VAT on the gross sales price. The VAT rates range up to 17%, 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 and VAT receivable net of payments in the accompanying financial statements. The VAT tax return is filed offsetting the payables against the receivables.

Stock-based compensation

The Company accounts for equity instruments issued in exchange for the receipt of goods or services from other than employees in accordance with the FASB's accounting standards regarding accounting for stock-based compensation and accounting for equity instruments that are issued to other than employees for acquiring or in conjunction with selling goods or services. Costs are measured at the estimated fair market value of the consideration received or the estimated fair value of the equity instruments issued, whichever is more reliably determinable. The value of equity instruments issued for consideration other than employee services is determined on the earlier of a performance commitment or completion of performance by the provider of goods or services as defined by these accounting standards. In the case of equity instruments issued to consultants, the fair value of the equity instrument is recognized over the term of the consulting agreement.

Advertising and promotion costs

Advertising and promotion costs are expensed as incurred, and amounted to \$131,600 and \$39,419 for three months ended June 30, 2011 and 2010, respectively. Advertising and promotion costs consist primarily of print and television advertisements.

Pre-opening costs

Expenditures related to the opening of new drugstores, other than expenditures for property and equipment, are expensed as incurred.

Vendor allowances

The Company accounts for vendor allowances by reducing the carrying value of inventories which are subsequently transferred to cost of goods sold when the inventories are sold, unless those allowances are specifically identified as reimbursements for advertising, promotion and other services, in which case they are recognized as a reduction of the related advertising and promotion or other service costs.

The Company recognized vendor allowances of \$72,805 and \$269,979 in cost of goods sold for the three months ended June 30, 2011 and 2010, respectively.

Distribution costs

Distribution costs represent the costs of transporting merchandise from warehouse to stores. These costs are expensed as incurred and are included in sales and marketing costs.

Operating leases

The Company leases premises for retail drugstores and offices under non-cancelable 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 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. Land leased from 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”), being the currency of the People’s Republic of China.

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 June 30, 2011 and March 31, 2011 were translated at 1 RMB to \$0.1547 USD and at 1 RMB to \$0.1527 USD, respectively. The average translation rates applied to income and cash flow statement amounts for the three months ended June 30, 2011 and 2010 were at 1 RMB to \$0.1539 USD and at 1 RMB to \$0.1467 USD, respectively.

Concentrations and credit risk

The Company’s operations are all carried out in the PRC, with over 95% of the sales coming from Hangzhou. Accordingly, the Company’s business, financial condition and results of operations may be influenced by the political, economic and legal environments in the PRC, and by the general state of the PRC’s economy. The Company’s operations are also subject to specific 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 environments and foreign currency exchange. The Company’s results may be adversely affected by changes in governmental policies with respect to laws and regulations, anti-inflationary measures, currency conversion and remittance abroad, and rates and methods of taxation, among other things.

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. Balances at financial institutions and state-owned banks within the PRC are not covered by insurance. As of June 30, 2011 and March 31, 2011, the Company had deposits totaling \$5,406,511 and \$7,068,093 that were not covered by insurance, respectively. To date, the Company has not experienced any losses in such accounts.

For the three months ended June 30, 2011 and 2010, all of the Company's sales and purchases arose in the PRC.

For the three months ended June 30, 2011, three vendors collectively accounted for 40% of the Company's total purchases, 40% of accounts payable and 14% of total purchase deposits. For the three months ended June 30, 2010, two vendors collectively accounted for 32% of the Company's total purchases and 26% of total purchase deposits.

Recently issued accounting pronouncements

In May 2011, the FASB and International Accounting Standards Board ("IASB") issued Accounting Standard Update ("ASU") No. 2011-04, Fair Value Measurement (Topic 820): Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs. ASU 2011-04 created a uniform framework for applying fair value measurement principles for companies around the world and clarified existing guidance in US GAAP. ASU 2011-04 is effective for the first reporting annual period beginning after December 15, 2011 and shall be applied prospectively. The Company does not expect the adoption of this ASU to have any material effect on its consolidated financial statements.

In June 2011, the FASB issued Comprehensive Income (Topic 220) — Presentation of Comprehensive Income (ASU No. 2011-05), which updates the Codification to require the presentation of the components of net income, the components of other comprehensive income (OCI) and total comprehensive income in either a single continuous statement of comprehensive income or in two separate, but consecutive statements of net income and comprehensive income. These updates do not affect the items reported in OCI or the guidance for reclassifying such items to net income. These updates to the Codification are effective for interim and annual periods beginning after December 15, 2011. The Company does not expect the implementation of this guidance to have a material impact on its consolidated financial statements.

Other accounting standards that have been issued or proposed by the FASB or other standards-setting bodies that do not require adoption until a future date are not expected to have a material impact on the Company's consolidated financial statements upon adoption.

Reclassifications

Certain prior period amounts have been reclassified to conform to the current period presentation. These reclassifications have no effect on net income or cash flows.

Note 3 – OTHER CURRENT ASSETS

Other current assets consist of the following:

| | June 30, 2011 | March 31, 2011 |
|--------------------------------|------------------|-------------------|
| Prepaid rental expenses | \$ 2,214,732 | \$ 1,316,626 |
| Lease rights transfer fees (1) | 391,243 | 380,981 |

| | | |
|----------------------------------|--------------|--------------|
| Security deposit with vendor | - | 4,581,132 |
| Prepays and other current assets | 111,398 | 166,148 |
| Advance to contractor | 1,856,400 | 1,919,380 |
| Total | \$ 4,573,773 | \$ 8,364,267 |

- (1) Lease rights transfer fees are paid by the Company to secure store rentals in coveted areas. These additional costs of acquiring the right to lease new store locations are capitalized and amortized over the period of the initial lease term.

Note 4 – PROPERTY AND EQUIPMENT

Property and equipment consisted of the following:

| | June 30, 2011 | March 31, 2011 |
|--------------------------------|------------------|-------------------|
| Leasehold improvements | \$ 4,487,807 | \$ 3,481,773 |
| Office equipment and furniture | 916,594 | 867,304 |
| Motor vehicles | 272,794 | 269,275 |
| Total | 5,677,195 | 4,618,352 |
| Less: Accumulated depreciation | (2,922,284) | (2,661,615) |
| Construction-in-progress | 6,107,926 | 3,514,695 |
| Property and equipment, net | \$ 8,862,837 | \$ 5,471,432 |

Construction-in-progress includes leasehold improvements in progress at two new store locations that the Company purchased and three new store locations that the Company leased as of June 30, 2011. These stores are currently under remodeling and are not in operation. In addition, we are renovating three existing stores opened in the past. No depreciation is provided for construction-in-progress until such time as the assets are completed and placed into service.

Total depreciation expense for property and equipment was \$224,718 and \$148,584 for the three months ended June 30, 2011 and 2010, respectively.

Note 5 – ADVANCES TO SUPPLIERS

Advances to suppliers consist of deposits with or advances to outside vendors for future inventory purchases. Most of the Company's vendors 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 June 30, 2011 and March 31, 2011, advances to suppliers amounted to \$14,786,933 and \$16,528,772, respectively. Historically, the Company has not experienced any losses as a result of these advances.

Note 6 – LONG TERM DEPOSITS, LANDLORDS

Long term deposits are money deposited with or advanced to landlords for securing retail store leases for which the Company does not anticipate applying or being returned within the next twelve months. Most of the Company's landlords require a minimum of nine months' rent being paid upfront plus additional deposits.

Note 7 – PREPAID - NONCURRENT

Prepaid – noncurrent consist of the following:

| | June 30, 2011 | March 31, 2011 |
|---|------------------|-------------------|
| Prepayment for lease of land use right – noncurrent (1) | \$ 5,530,525 | \$ 5,497,358 |
| Lease rights transfer fees-noncurrent (2) | 539,852 | 578,120 |
| Deposit made to secure business acquisition (3) | 4,770,639 | - |
| Total | \$ 10,841,016 | \$ 6,075,478 |

- (1) This is a payment made to the local government in connection with entering into a 30-year operating land lease agreement.
- (2) Lease rights transfer fees are paid by the Company to secure store rentals in coveted areas. These additional costs of acquiring the right to lease new store locations are capitalized and amortized over the period of the initial lease term.
- (3) This is a refundable advance payment made to the owners of Zhejiang Jiuxin Medicine Co., Ltd. ("Jiuxin Medicine") to acquire their equity interests in Jiuxin Medicine. In April 2011, the business license of Jiuxin Medicine was transferred to Jiuzhou Pharmacy. The Company is currently finalizing the payment terms with the sellers, and the operating control of Jiuxin Medicine has not been transferred to the Company.

Note 8 – TAXES

Income tax

| Entity | Income Tax Jurisdiction |
|-----------------------|-------------------------|
| Jo-Jo Drugstores | United States |
| Renovation | Hong Kong |
| Jiuxin Management | PRC |
| Shouantang Technology | PRC |
| Jiuxin Qianhong | PRC |
| Quannuo Technology | PRC |
| Hangzhou Quannuo | PRC |
| Jiuzhou Pharmacy | PRC |
| Jiuzhou Clinic | PRC |
| Jiuzhou Service | PRC |
| Shanghai Lydia | PRC |
| Tonglu Lydia | PRC |

The following table reconciles the U.S. statutory tax rates to the Company's effective tax rate for the three months ended June 30, 2011 and 2010:

| | 2011 | 2010 |
|---|------|------|
| U.S. Statutory rates | 34% | 34% |
| Foreign income not recognized in the U.S. | (34) | (34) |
| China income taxes | 25 | 25 |
| Other (1) | 3 | 4 |
| Effective tax rate | 28% | 29% |

- (1) The 3% and 4% for the three months ended June 30, 2011 and 2010, respectively, represent expenses incurred by the Company that were 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 2010. As of June 30, 2011, the estimated net operating loss carryforwards for U.S. income tax purposes amounted to \$993,000 which may be available to reduce future years' taxable income. These carryforwards will expire, if not utilized by 2031. Management believes that the realization of the benefits arising from this loss appears to be uncertain due to the Company's limited operating history and continuing losses for U.S. income tax purposes. Accordingly, the Company has provided a 100% valuation allowance at June 30, 2011. The net change in the valuation allowance for the three months ended June 30, 2011 was an increase of approximately \$61,000. Management reviews this valuation allowance periodically and makes adjustments as necessary. The Company did not have operating loss as of June 30, 2010.

The Company had cumulative undistributed earnings of foreign subsidiaries of approximately \$29 million as of June 30, 2011, which are included in consolidated retained earnings and will continue to be indefinitely reinvested in international operations. Accordingly, no provision has been made for U.S. deferred taxes related to future repatriation of these earnings.

Value added tax

VAT on sales and on purchases amounted to \$3,483,909 and \$2,264,888 for the three months ended June 30, 2011, and \$2,454,477 and \$1,987,825 for the three months ended June 30, 2010, respectively.

Sales and purchases are recorded net of VAT collected and paid as the Company acts as an agent for the government. VAT taxes are not impacted by the income tax holiday.

Taxes payable at June 30 2011 and March 31, 2011 consisted of the following:

| | June 30, 2011 | March 31, 2011 |
|---------------------|------------------|-------------------|
| VAT | \$ 353,434 | \$ 421,562 |
| Income tax | 1,256,470 | 1,146,453 |
| Others | 43,733 | 56,543 |
| Total taxes payable | \$ 1,653,637 | \$ 1,624,558 |

Note 9 – 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 \$80,763 and \$13,076 in employment benefits and pension for the three months ended June 30, 2011 and 2010, respectively.

Note 10 – RELATED PARTY TRANSACTIONS AND ARRANGEMENTS

Amounts receivable from and payable to related parties are summarized as follows:

| | June 30, 2011 | March 31, 2011 |
|------------------------------|------------------|-------------------|
| Amount due to directors (1): | \$ 800,058 | \$ 800,058 |

- (1) As of June 30, 2011 and March 31, 2011, amount due to directors represents advances from the Owners to Jiuxin Management to enable Jiuxin Management to meet its approved PRC registered capital requirements.

As of June 30, 2011 and March 31, 2011, notes payable totaling \$2,273,530 and \$1,609,336 were secured by the personal properties of certain of the Company's shareholders, respectively.

One of the Company's retail spaces and its corporate office are leased from Lei Liu, a director of the Company, under long-term operating lease agreements from August 2010 to August 2012 and from January 2011 to December 2012, respectively. The rent expense amounted to \$46,170 and \$42,531 for the three months ended June 30, 2011 and 2010, respectively. Rent paid to Mr. Liu amounted to \$0 and \$44,190 for the three months ended June 30, 2011 and 2010, respectively.

Note 11 – PURCHASE OPTION DERIVATIVE LIABILITY

In connection with the public offering of the Company's common stock that closed on April 28, 2010, the Company issued to its underwriters, Madison Williams and Company and Rodman & Renshaw, LLC, an option for \$100 to purchase up to a total of 105,000 shares of common stock (3% of the shares sold in the public offering) at \$6.25 per share (125% of the price of the shares sold in the public offering). The option is exercisable commencing on October 23, 2010 and expires on April 22, 2015.

The Company is treating the common shares underlying the option as a derivative liability as the strike price of the option is denominated in U.S. dollars, a currency other than the Company's functional currency, the Chinese RMB. As a result, the option is not considered indexed to the Company's own stock, and as such, all future changes in the fair value of the option are recognized currently in earnings until such time as the option is exercised or expired.

On April 22, 2010, the issue date of the option, the Company classified the fair value of this option as a liability resulting in a decrease of additional paid-in capital of \$402,451 and the establishment of \$402,451 in liability to recognize the option's fair value. The Company recognized a gain of \$62,632 and \$57,944 from the change in fair value of the option liability for the three months ended June 30, 2011 and 2010, respectively.

This option does not trade in an active securities market, and as such, the Company estimates its fair value using the Black-Scholes Option Pricing Model (the "Black-Scholes Model") on the date that the option was originally issued and as of June 30, 2011 using the following assumptions:

| | Underwriter Purchase Option | |
|-------------------------|-----------------------------|----------------------|
| | April 22, 2010 | June 30, 2011 (1) |
| Stock price | \$ 4.78 | \$ 1.91 |
| Exercise price | \$ 6.25 | \$ 6.25 |
| Annual dividend yield | 0% | 0% |
| Expected term (years) | 5.00 | 3.81 |
| Risk-free interest rate | 2.57% | 0.81% |
| Expected volatility | 120% | 98% |

(1) As of June 30, 2011, the option to purchase 105,000 shares of common stock had not been exercised.

Expected volatility is based on historical volatility. Historical volatility was computed using daily pricing observations for recent periods that correspond to the term of the option. The Company believes this method produces an estimate that is representative of future volatility over the expected term of this option. The expected life is based on the remaining term of the option. The risk-free interest rate is based on U.S. Treasury securities according to the remaining term of the option.

As required by the FASB's accounting standards, financial assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement. Depending on the product and the terms of the transaction, the fair values of option liability are modeled using a series of techniques, including closed-form analytic formula, such as the Black-Scholes Model, which does not entail material subjectivity because the methodology employed does not necessitate significant judgment, and the pricing inputs are observed from actively quoted markets.

The fair value of the 105,000 shares underlying the option outstanding as of June 30, 2011 was determined using the Black-Scholes Model, with certain inputs significant to the valuation methodology as level 2 inputs, and the Company

recorded the change in fair value in earnings. As a result, the option liability is carried on the consolidated balance sheets at fair value.

The following table sets forth, by level within the fair value hierarchy, the Company's financial assets and liabilities that were accounted for at fair value as of June 30, 2011:

| | Carrying Value at June 30, 2011 | Fair Value Measurement at June 30, 2011 | | |
|--------------------------------------|--|---|-----------|---------|
| | | Level 1 | Level 2 | Level 3 |
| Purchase option derivative liability | \$90,594 | \$ — | \$ 90,594 | \$ — |

Note 12 – STOCKHOLDER’S EQUITY

Common stock

On April 9, 2010, the Company effected a 1-for-2 reverse split of its issued and outstanding shares of common stock and a proportional reduction of its authorized shares of common stock. All share and per share amounts used in the Company’s consolidated financial statements and accompanying notes have been retroactively restated to reflect the 1-for-2 reverse stock split.

On April 28, 2010, the Company closed a public offering of 3.5 million shares of common stock at \$5.00 per share with gross proceeds of approximately \$17.5 million.

Stock-based compensation

On March 15, 2010, the Company entered into a service agreement with a non-executive director and agreed to issue 6,897 shares of restricted common stock for his annual service. The terms of the service agreement has been continued, and 11,268 shares of restricted common stock will be issued accordingly. The trading value of the Company’s common stock on March 15, 2011 and 2010 was \$3.55 and \$5.80, respectively. \$9,973 and \$9,976 were charged to general and administrative expense for the three months ended June 30, 2011 and 2010, respectively.

On May 1, 2010, the Company agreed to issue 2,340 shares of common stock to its legal counsel as partial payment for six months of legal services. The trading value of the Company’s common stock on May 1, 2010 was \$4.80. \$3,744 was charged to general and administrative expense for the three months ended June 30, 2010.

On May 1, 2010, the Company agreed to issue 6,000 shares of common stock to an employee as partial payment for compensation. The trading value of the Company’s common stock on May 1, 2010 was \$4.80. \$2,400 and \$4,800 were charged to general and administrative expense for the three months ended June 30, 2011 and 2010, respectively.

On May 14, 2010, the Company entered into an agreement pursuant to which the Company agreed to issue 10,000 shares of restricted common stock to its chief financial officer upon the adoption of a stock incentive plan (the “Plan”) as part of his annual compensation. On April 28, 2011, the employment agreement was renewed and 4,613 shares of restricted common stock will be issued. The trading value of the Company’s common stock on April 28, 2011 and May 14, 2010 were \$2.71 and \$4.66, respectively. \$11,733 and \$8,169 was charged to general and administrative expense for the three months ended June 30, 2011 and 2010, respectively.

The Company also agreed under the agreement with the chief financial officer to issue 4,000 shares of restricted common stock from the Plan as a bonus. The trading value of the Company’s common stock on May 14, 2010 was \$4.66. \$18,640 was charged to general and administrative expense for the three months ended June 30, 2010.

On November 1, 2010, the Company agreed to issue 2,340 shares of common stock to its legal counsel as partial payment for six months of legal services. On May 1, 2011, the Company agreed to issue an additional 2,340 shares of common stock to its legal counsel as partial payment for another six months of legal services. The trading value of the Company’s common stock on May 1, 2011 and November 1, 2010 were \$2.71 and \$5.00, respectively. \$4,042 was recorded as service compensation expense for the three months ended June 30, 2011.

Statutory reserve

Statutory reserves represent restricted retained earnings. Based on their legal formation, the Company is required to set aside 10% of its net income as reported in their statutory accounts on an annual basis to the Statutory Surplus

Reserve Fund (the “Reserve Fund”). 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 dividend 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 months ended June 30, 2011 and 2010, the Company did not make appropriations to the statutory reserves. The other subsidiaries were still in the development stage and had not allocated any contribution to the statutory surplus reserve fund.

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 13 – EARNINGS 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 earnings per share computation:

| | Three months Ended June 30, | |
|---|--------------------------------|--------------|
| | 2011 | 2010 |
| Net income for earnings per share | \$ 3,242,729 | \$ 2,152,464 |
| Weighted average shares used in basic computation | 13,532,240 | 12,653,848 |
| Diluted effect of purchase options | - | - |
| Weighted average shares used in diluted computation | 13,532,240 | 12,653,848 |
| Earnings per share – Basic and diluted: | \$ 0.24 | \$ 0.17 |

For the three months ended June 30, 2011, 105,000 shares underlying outstanding purchase options were excluded from the diluted earnings per share calculation as they are anti-dilutive.

Note 14 – SEGMENTS

The Company sells prescription and over-the-counter medicines, TCM, dietary supplement, medical devices, and sundry items. The class of customers, selling practice and distribution process are the same for all products. Based on qualitative and quantitative criteria established by the FASB's accounting standard, "Disclosures about Segments of an Enterprise and Related Information," the Company considers itself to be operating within one reportable segment.

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 by main products is as follows:

| | Three Months Ended June 30, | |
|------------------------------|--------------------------------|---------------|
| | 2011 | 2010 |
| Prescription Drugs | \$ 9,721,466 | \$ 6,162,598 |
| Over-The-Counter (OTC) Drugs | 6,283,486 | 5,441,859 |
| Nutritional Supplements | 2,192,635 | 1,731,081 |
| TCM | 2,576,311 | 1,290,891 |
| Sundry Products | 306,407 | 371,263 |
| Medical Devices | 347,554 | 209,736 |
| Total | \$ 21,427,859 | \$ 15,207,428 |

Note 15 – BUSINESS COMBINATION

On November 19, 2010, Shouantang Technology entered into equity ownership transfer agreements with the owners of Quannuo Technology to acquire 100% of equity interests of Quannuo Technology and its subsidiary, Hangzhou Quannuo. Quannuo Technology develops software for online drugstores.

Shouantang Technology acquired all assets and assumed all liabilities of Quannuo Technology. The consideration of the transaction included a cash payment of \$606,800 (RMB 4,000,000) to pay off outstanding loans with the former owners, with the excess capitalized by the Company as intangible assets of approximately \$443,125. Amortization expense of the intangible assets was \$37,463 and \$0 for the three months ended June 30, 2011 and 2010.

Note 16 – COMMITMENTS AND CONTINGENCIES

Operating lease commitments

The Company recognizes lease expense 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 that it has leased from a local government to be used potentially for the cultivation of Chinese medicinal herbs.

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

| Periods ending June 30, | Amount |
|-------------------------|--------------|
| 2012 | \$ 2,859,600 |
| 2013 | 2,952,328 |
| 2014 | 2,596,382 |
| 2015 | 2,131,662 |
| 2016 | 1,621,887 |
| Thereafter | 1,050,461 |

Total rent expense amounted to \$731,746 and \$432,428 for the three months ended June 30, 2011 and 2010, respectively.

As of June 30, 2011 and 2010, prepayment on retail and office leases amounted to \$2,214,732 and \$1,316,626, respectively.

Note 17 – SUBSEQUENT EVENTS

On August 1, 2011, the Company entered into an agreement with Worldwide Officers, Inc., a California corporation (“WOI”), to memorialize the terms under which Mr. Bennet P. Tchaikovsky had been serving as the Company’s chief financial officer from April 28, 2011 to August 1, 2011. As memorialized under the agreement, WOI is compensated from April 28, 2011 to August 1, 2011 with \$25,000 and 4,613 shares of the Company’s common stock under the Plan (“WOI Shares”), as well as reimbursement of expenses. In connection with the WOI Shares, the Company and WOI entered into a restricted stock award agreement dated as of August 1, 2011.

On August 1, 2011, Mr. Tchaikovsky resigned as the Company’s chief financial officer, and Mr. Shike Zhu resigned from the Company’s board of directors. Mr. Ming Zhao was appointed to replace Mr. Tchaikovsky as chief financial officer, and Mr. Tchaikovsky was appointed to the board of directors to replace Mr. Zhu.

Under Mr. Zhao’s employment agreement with the Company dated as of August 1, 2011, Mr. Zhao will serve as the chief financial officer for a term of two years commencing August 1, 2011, for annual compensation of \$100,000, payable in monthly installments, as well as a one-time grant of 40,000 shares of the Company’s common stock (“CFO Shares”) under the Plan that will vest in eight equal quarterly installments over the two year agreement period beginning on August 1, 2011. In connection with the CFO Shares, the Company and Mr. Zhao entered into a restricted stock award agreement dated as of August 1, 2011.

Under Mr. Tchaikovsky’s agreement with the Company dated as of August 1, 2011, Mr. Tchaikovsky will receive an annualized compensation of \$40,000 as a director, including \$30,000 in cash payable in twelve equal monthly installments on the first day of each month commencing August 1, 2011, and \$10,000 of shares of the Company’s common stock under the Plan (the “Director Shares”). In connection with the Director Shares, the Company and Mr. Tchaikovsky entered into a restricted stock award agreement dated as of August 1, 2011.

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

The following management's discussion and analysis should be read in conjunction with our 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, 2011 and filed with the SEC on June 29, 2011. 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 at various pertinent dates and for pertinent periods.

Overview

We are primarily an operator of retail pharmacies based in Zhejiang Province, China. Our drugstores provide customers with a wide variety of medicinal products, including prescription and OTC drugs, nutritional supplements, traditional Chinese medicine ("TCM"), personal care products, family care products, medical devices, as well as convenience products including consumable, seasonal and promotional items. We briefly offered baijiu, or Chinese white liquor, at some of our pharmacies from December 2010 to February 2011. Each store typically carries approximately 2,500 to 7,000 different products. In addition to these products, we have licensed doctors of both western medicine and TCM onsite for consultation, examination and treatment of common ailments at scheduled hours. Our stores presently average approximately 290 to 300 square meters.

In addition to pharmacies and medical clinics, we plan to distribute herbal plants being cultivated on our leased land at our pharmacies and to third parties. In August 2010, we established Hangzhou Jiuxin Qianhong Agriculture Development Co., Ltd. ("Jiuxin Qianhong") as a wholly-owned subsidiary to operate this cultivation project. Currently, more than ten herbal plants, including fructus rubi, white atractylodes rhizome and atractylodes macrocephala, are being cultivated on approximately 48 acres, which we expect to harvest in the latter half of 2011 through early 2012.

We have also been operating an online drugstore (www.dada360.com) that sells non-prescription drugs (including over-the-counter drugs and nutritional supplements), since May 2010. In July 2010, we established Zhejiang Shouantang Pharmaceutical Technology Co., Ltd. ("Shouantang Technology") as a wholly-owned subsidiary and acquired Zhejiang Quannuo Internet Technology Co., Ltd. ("Quannuo Technology") in November 2010 to operate the website and provide software and technical support. As a part of our acquisition of Quannuo Technology, we also acquired its wholly-owned subsidiary, Hangzhou Quannuo Grand Pharmacy Co., Ltd. ("Hangzhou Quannuo"), and the "Quannuo Grand Pharmacy" store. Other than activities relating to investing and financing the working capital of Quannuo Technology and coordinating short-term inter-company loans, Shouantang Technology has had no separate operations of its own as of June 30, 2011. In June 2011, we established Tonglu Lydia Agriculture Development Co., Ltd. ("Tonglu Lydia") as a wholly-owned subsidiary of Shouantang Technology to undertake herbal cultivation similar to that of Jiuxin Qianhong. As of the date of this report, however, such project has not commenced, and Tonglu Lydia currently has no operation.

Jiuzhou Pharmacy's subsidiary Hangzhou Kuaileren Grand Pharmacy Co., Ltd. ("Kuaileren") was formally dissolved on April 9, 2011 and its assets transferred to Jiuzhou Pharmacy. Prior to its dissolution, Kuaileren operated a "Kuaileren Grand Pharmacy" store, which now operates as a "Jiuzhou Grand Pharmacy" store.

On April 15, 2011, Jiuzhou Pharmacy entered into an equity ownership transfer agreement with the owners of Zhejiang Jiuxin Medicine Co., Ltd. ("Jiuxin Medicine") to acquire their equity interests in Jiuxin Medicine for RMB 50 million. Jiuxin Medicine is licensed to transport and store pharmaceutical products, and we are negotiating to acquire this company in order to carry out such functions internally and to use Jiuxin Medicine's facility as our distribution center. In April 2011, the business license of Jiuxin Medicine was transferred to Jiuzhou Pharmacy. As of the date of this report, however, we are still finalizing the payment terms with the sellers.

Critical Accounting Policies and Estimates

In preparing our 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. We believe the following accounting policies involve the most significant judgment and estimates used in the preparation of our financial statements. We have not made any material changes in the methodology used in our accounting policies which are consistent with those discussed in our annual report on Form 10-K for the year ended March 31, 2011.

Recent Accounting Pronouncements

In May 2011, the FASB and International Accounting Standards Board (“IASB”) issued Accounting Standard Update (“ASU”) No. 2011-04, Fair Value Measurement (Topic 820): Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs. ASU 2011-04 created a uniform framework for applying fair value measurement principles for companies around the world and clarified existing guidance in US GAAP. ASU 2011-04 is effective for the first reporting annual period beginning after December 15, 2011 and shall be applied prospectively. We do not expect the adoption of this ASU to have any material effect on our consolidated financial statements.

In June 2011, the FASB issued Comprehensive Income (Topic 220) — Presentation of Comprehensive Income (ASU No. 2011-05), which updates the Codification to require the presentation of the components of net income, the components of other comprehensive income (OCI) and total comprehensive income in either a single continuous statement of comprehensive income or in two separate, but consecutive statements of net income and comprehensive income. These updates do not affect the items reported in OCI or the guidance for reclassifying such items to net income. These updates to the Codification are effective for interim and annual periods beginning after December 15, 2011. We do not expect the implementation of this guidance to have a material impact on our consolidated financial statements.

Results of Operations

The following table summarizes our results of operations for the three months ended June 30, 2011 and 2010.

| | Three Months Ended June 30 | | | | | | | |
|-------------------------------------|-------------------------------|--|------------------|--|---------------|--|------------------|--|
| | 2011 | | Percentage of | | 2010 | | Percentage of | |
| | Amount | | total revenue | | Amount | | total revenue | |
| Revenues | \$ 21,427,859 | | 100.0 % | | \$ 15,207,428 | | 100.0 % | |
| Gross Profit | \$ 6,869,323 | | 32.1 % | | \$ 4,613,896 | | 30.3 % | |
| Selling Expenses | \$ 1,378,300 | | 6.4 % | | \$ 823,358 | | 5.4 % | |
| General and Administrative Expenses | \$ 1,074,783 | | 5.0 % | | \$ 773,762 | | 5.1 % | |
| Income from Operations | \$ 4,416,240 | | 20.6 % | | \$ 3,016,776 | | 19.8 % | |
| Other Income (Expense), Net | \$ 19,420 | | 0.1 % | | \$ (57,532) | | (0.4) % | |

Change in Fair Value of
Purchase Option

| | | | | | | | | |
|----------------------|----|-----------|------|---|----|-----------|------|---|
| Derivative Liability | \$ | 62,632 | 0.3 | % | \$ | 57,944 | 0.4 | % |
| Income Tax Expenses | \$ | 1,255,563 | 5.9 | % | \$ | 864,724 | 5.7 | % |
| Net Income | \$ | 3,242,729 | 15.1 | % | \$ | 2,152,464 | 14.2 | % |

Revenue. Our revenue increased by \$6,220,431 or 40.9% to \$21,427,859 for the three months ended June 30, 2011 from \$15,207,428 for the three months ended June 30, 2010 primarily as a result of increased same store sales. Revenue from our 25 locations that were opened prior to April 1, 2010 increased \$4,535,527 or 31.9% period over period. This increase was mainly attributed to sales of pharmaceutical products covered government-sponsored medical insurance programs. All of our store locations opened prior to April 1, 2010 are licensed to accept medical insurance, and sales at such locations have steadily increased as such insurance programs covered more drugs and participants. After we open a drugstore we must wait one year to apply for the license to accept government medical insurance. After a store has been open for one year we apply to accept government medical insurance at that store, if practicable. Revenues also increased from operating additional store locations. We operated 57 stores as of June 30, 2011, as compared to 31 stores as of June 30, 2010. We opened 6 stores during the three months ended June 30, 2011. We anticipate that our overall revenue will continue to increase as we open additional stores and our maturing stores are able to accept government insurance.

Gross Profit. Our gross profit increased by \$2,255,427 or 48.9% to \$6,869,323 for the three months ended June 30, 2011 from \$4,613,896 for the three months ended June 30, 2010. Our gross margin increased period over period from 30.3% to 32.1% partially as a result from selling additional TCM products that have a higher gross margin than our other products.

Selling Expenses. Our selling expenses increased by \$554,942 or 67.4% to \$1,378,300 for the three months ended June 30, 2011 from \$823,358 for the three months ended June 30, 2010. The increase was primarily a result of operating 57 store locations as compared to 31 stores that we operated as of June 30, 2010. Selling expenses as a percentage of our revenue increased from 5.4% to 6.4% period over period. We expect that our selling expenses will continue to increase as we continue to expand our store network.

General and Administrative Expenses. Our general and administrative expenses increased by \$301,021 or 38.9% to \$1,074,783 for the three months ended June 30, 2011 from \$773,762 for the three months ended June 30, 2010. General and administrative expenses as a percentage of our revenue slightly decreased from 5.1% to 5.0% period over period. The increase in absolute dollars relates to operating additional drugstores. As we continue to open drugstores, further develop our infrastructure, and incur expenses related to being a public company, we anticipate that our general and administrative expenses will increase in absolute dollars as well as a percentage of total revenues.

Income from Operations. As a result of our increased gross profit, our income from operations increased by \$1,399,464 or 46.4% to \$4,416,240 for the three months ended June 30, 2011 from \$3,016,776 for the three months ended June 30, 2010. Our operating margin for the three months ended June 30, 2011 and 2010 was 20.6% and 19.8%, respectively.

Income Tax. Our income tax expense increased to \$1,255,563 for the three months ended June 30, 2011 from \$864,724 for the three months ended June 30, 2010, as a result of increased income from operations. Our effective tax rate decreased from 29% to 28% period over period mainly as a result of certain expenses that we incurred in the U.S. as a public company not being deductible for PRC tax purposes that were incurred during the three months ended June 30, 2011 and 2010.

Net Income. As a result of the foregoing, our net income increased by \$1,090,265 or 50.7% to \$3,242,729 for the three months ended June 30, 2011 from \$2,152,464 for the three months ended June 30, 2010.

Liquidity

In summary, our cash flows for the periods indicated are as follows:

| | Three months ended June 30 | |
|---|----------------------------|---------------|
| | 2011 | 2010 |
| Net cash provided by (used in) operating activities | \$ 9,912,293 | \$ (65,804) |
| Net cash used in investing activities | \$ (8,273,420) | \$ (442,709) |
| Net cash (used in) provided by financing activities | \$ (1,758,015) | \$ 15,461,665 |

For the three months ended June 30, 2011, we generated cash from operating activities of \$9,912,293, as compared to using cash in operating activities of \$65,804 for the three months ended June 30, 2010. The increase is primarily attributable to a partial liquidation of our advances to suppliers and a return of a security deposit with a vendor totaling \$4,581,132 during the three months ended June 30, 2011.

We used \$8,273,420 in investing activities during the three months ended June 30, 2011, as compared to cash used in investing activities of \$442,709 during the three months ended June 30, 2010 as a result of payments on construction-in-progress of \$2,534,126 and deposit to secure an acquisition of a drug distribution business of \$4,770,639 during the three months ended June 30, 2011.

Cash used in financing activities was \$1,758,015 for the three months ended June 30, 2011, as compared to cash provided by financing activities of \$15,461,665 for the three months ended June 30, 2010. The decrease is due to the equity offering which raised \$15.7 million in net proceeds, after deducting underwriter discount, commission, and offering expenses during the three months ended June 30, 2010.

As of August 11, 2011, we had cash of approximately \$5,484,439. Our total current assets as of June 30, 2011 were \$33,251,497 and our total current liabilities were \$10,041,893, which resulted in a net working capital of \$23,209,604

as of June 30, 2011.

Capital Resources

In April 2010, we completed a public offering of 3.5 million shares of our common stock at a price of \$5.00 per share resulting in gross proceeds of \$17.5 million and net proceeds of \$15.7 million after deducting commissions and all other expenses.

During the next ninety days, we may complete our acquisition of Jiuxin Medicine that may require a cash payment in addition to the deposit that we already made, and we have an obligation to contribute RMB 8,000,000 to complete the registered capital requirement for Quannuo Technology. We believe that with our current working capital, we will be able to meet these obligations and maintain our operations for at least 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 June 30, | |
| 2012 | \$ 2,859,600 |
| 2013 | 2,952,328 |
| 2014 | 2,596,382 |
| 2015 | 2,131,662 |
| 2016 | 1,621,887 |
| Thereafter | 1,050,461 |

Logistics Services Commitments

As of June 30, 2011, we used a third party service provider, Yingte Logistics, to accept goods from our suppliers and to deliver the goods to our store locations. Pursuant to our one-year agreement with Yingte Logistics entered into on January 1, 2011, we are obligated to pay 1% of the purchase price of the goods received from our suppliers by Yingte Logistics during the term of the agreement, from January 1, 2011 to December 31, 2011, with a contractual minimum of 3.9 million RMB.

We terminated our agreement with Yingte Logistics in April 2011, and now use Jiuxin Medicine's facility as our distribution center. As we are still in the process of negotiating the acquisition of Jiuxin Medicine, we now engage Jiuxin Medicine as our logistics service provider and pay for the goods it delivers. Currently, Jiuxin Medicine contracted Yingte to deliver the goods to our store locations. Once we complete the acquisition of Jiuxin Medicine, we intend to carry out logistics functions internally.

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 in the PRC and the HJ Group maintain their books and records in Renminbi ("RMB"), the lawful currency of the PRC. In general, for consolidation purposes, we translate their assets and liabilities into US\$ 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 US\$ for the purposes of preparing the consolidated financial statements or otherwise disclosed in this report were as follows:

| | June 30, 2011 | March 31, 2011 | June 30, 2010 |
|--|------------------|-------------------|-------------------|
| Balance sheet items, except for the registered and paid-up capital, as of end of period/year | USD1: RMB 0.1547 | USD1: RMB 0.1527 | USD1: RMB 0.14730 |
| Amounts included in the statement of operations, statement of changes in stockholders' equity and statement of cash flows for the period/ year ended | USD1: RMB 0.1539 | USD1: RMB 0.14909 | USD1: RMB 0.14673 |

No representation is made that RMB amounts have been, or would be, converted into U.S. Dollars at the above rates.

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.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

As of June 30, 2011, we carried out an evaluation, under the supervision and with the participation of our management, including our chief executive officer and chief financial officer, of 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 that 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.

In our annual report on Form 10-K for the year ended March 31, 2011, we reported certain weaknesses involving control activities, primarily accounting and finance personnel weaknesses. Our current accounting staff members remain relatively inexperienced in U.S. GAAP-based reporting and require additional training so as to meet with the higher demands necessary to fulfill the requirements of U.S. GAAP-based reporting and SEC rules and regulations.

The Company's management has identified the steps it believes are necessary to address the weaknesses described above, and expect that we will satisfactorily address the control deficiencies and weaknesses relating to these matters by the end of our fiscal year ending March 31, 2012, although there can be no assurance that compliance will be achieved in this time frame.

On August 1, 2011, we retained Mr. Ming Zhao as our chief financial officer. Mr. Zhao is a U.S. licensed certified public accountant, has financial reporting experience, and works on a fulltime basis from our headquarters in Hangzhou. We believe that Mr. Zhao will be able to assist the Company in addressing our accounting and finance personnel weaknesses; however, until an independent evaluation is performed, we cannot give assurance that his hiring alone will remedy such internal control weaknesses.

Management, including our chief executive officer and our chief financial officer, does not expect that our disclosure controls and internal controls will prevent errors and omissions, even as the same are improved to address any deficiencies and/or weaknesses. A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Over time, controls may become inadequate because of changes in conditions or deterioration in the degree of compliance with policies or procedures. Further, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and errors and omissions, if any, within the Company have been detected. These inherent limitations include the realities that judgments in decision-making can be faulty, and that breakdowns can occur because of simple error or mistake. Additionally, controls can be circumvented by the individual acts of some persons, by collusion of two or more people, or by management override of the control.

Our financial reporting process includes extensive procedures we undertake in order to obtain assurance regarding the reliability of our published financial statements, notwithstanding the material weaknesses in internal control. As a result, management, to the best of its knowledge, believes that (i) this report does not contain any untrue statements of a material fact or omits any material fact and (ii) the financial statements and other financial information included in this report have been prepared in conformity with U.S. GAAP and fairly present in all material aspects our financial condition, results of operations, and cash flows.

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 1. Legal Proceedings.

Except as described below, we know of no material, existing or pending legal proceedings against us, nor are we involved as a plaintiff in any material proceeding or pending litigation. There are no proceedings in which any of our directors, officers or affiliates, or any registered or beneficial stockholder, is an adverse party or has a material interest

adverse to our company.

On December 8, 2009, Jiuzhou Pharmacy filed suit against The Ventana Group, LLC and Michael Hom in the California Superior Court for the County of San Mateo (Case Number CV490272), alleging breach of contract of an agreement entered into with the defendants in 2008 and seeking damages of \$25,000. The suit was subsequently amended to remove Mr. Hom as a defendant. In May 2010, Jiuzhou Pharmacy sought for default judgment against the remaining defendant, which was granted on July 14, 2010. Jiuzhou Pharmacy is in the process of executing the judgment against the defendant.

Item 1A. Risk Factors.

As of and for the three months ended June 30, 2011, there were no material changes in our risk factors from those disclosed in Part I, Item 1A, of our annual report on Form 10-K as of and for the year ended March 31, 2011.

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

None

Item 3. Defaults upon Senior Securities.

None

Item 4. Reserved.

Item 5. Other Information.

None

Item 6. Exhibits.

EXHIBIT INDEX

| Exhibit Number | Description |
|----------------|--|
| 2 | Share Exchange Agreement among Kerrisdale Mining Corporation (“Kerrisdale”), certain of its stockholders, Renovation Investment (Hong Kong) Co., Ltd. (“Renovation”) and its shareholders dated September 17, 2009 (3) |
| 3.1 | Articles of Incorporation of Kerrisdale (1) |
| 3.2 | Certificate of Amendment to Articles of Incorporation of Kerrisdale filed with the Nevada Secretary of State on July 14, 2008 (2) |
| 3.3 | Articles of Merger between Kerrisdale Mining and China Jo-Jo Drugstores, Inc. filed with the Nevada Secretary of State on September 22, 2009 (3) |
| 3.4 | Bylaws (1) |
| 3.5 | Text of Amendments to the Bylaws (2) |
| 3.6 | Certificate of Change Pursuant to NRS 78.209 with an effective date of April 9, 2010 (7) |
| 4.1 | Specimen of Common Stock Certificate (1) |
| 4.2 | 2010 Equity Incentive Plan (10) |
| 10.1 | Consulting Services Agreement between Zhejiang Jiuxin Investment Management Co., Ltd. (“Jiuxin Management”) and Hangzhou Jiuzhou Grand Pharmacy Chain Co., Ltd. (“Jiuzhou Pharmacy”) dated August 1, 2009 (3) |
| 10.2 | Operating Agreement among Jiuxin Management, Jiuzhou Pharmacy and its owners dated August 1, 2009 (3) |
| 10.3 | Equity Pledge Agreement among Jiuxin Management, Jiuzhou Pharmacy and its owners dated August 1, 2009 (3) |
| 10.4 | Option Agreement among Jiuxin Management, Jiuzhou Pharmacy and its owners dated August 1, 2009 (3) |
| 10.5 | Voting Rights Proxy Agreement among Jiuxin Management, Jiuzhou Pharmacy and its owners dated August 1, 2009 (3) |
| 10.6 | Consulting Services Agreement between Jiuxin Management and Hangzhou Jiuzhou Clinic of Integrated Traditional and Western Medicine (General Partnership) (“Jiuzhou Clinic”) dated August 1, 2009 (3) |
| 10.7 | Operating Agreement among Jiuxin Management, Jiuzhou Clinic and its owners dated August 1, 2009 (3) |
| 10.8 | Equity Pledge Agreement among Jiuxin Management, Jiuzhou Clinic and its owners dated August 1, 2009 (3) |
| 10.9 | Option Agreement among Jiuxin Management, Jiuzhou Clinic and its owners dated August 1, 2009 (3) |
| 10.10 | Voting Rights Proxy Agreement among Jiuxin Management, Jiuzhou Clinic and its owners dated August 1, 2009 (3) |
| 10.11 | Consulting Services Agreement between Jiuxin Management and Hangzhou Jiuzhou Medical & Public Health Service Co., Ltd. (“Jiuzhou Service”) dated August 1, 2009 (3) |
| 10.12 | Operating Agreement among Jiuxin Management, Jiuzhou Service and its owners dated August 1, 2009 (3) |
| 10.13 | Equity Pledge Agreement among Jiuxin Management, Jiuzhou Service and its owners dated August 1, 2009 (3) |
| 10.14 | Option Agreement among Jiuxin Management, Jiuzhou Service and its owners dated August 1, 2009 (3) |
| 10.15 | Voting Rights Proxy Agreement among Jiuxin Management, Jiuzhou Service and its owners dated August 1, 2009 (3) |

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- 10.16 Amendment to Consulting Services Agreement between Jiuxin Management and Jiuzhou Pharmacy dated October 27, 2009 (4)
- 10.17 Amendment to Operating Agreement between Jiuxin Management and Jiuzhou Pharmacy dated October 27, 2009 (4)
- 10.18 Amendment to Option Agreement between Jiuxin Management and Jiuzhou Pharmacy dated October 27, 2009 (4)
- 10.19 Amendment to Voting Rights Proxy Agreement between Jiuxin Management and Jiuzhou Pharmacy dated October 27, 2009 (4)
- 10.20 Amendment to Consulting Services Agreement between Jiuxin Management and Jiuzhou Clinic dated October 27, 2009 (4)
- 10.21 Amendment to Operating Agreement between Jiuxin Management and Jiuzhou Clinic dated October 27, 2009 (4)
- 10.22 Amendment to Option Agreement between Jiuxin Management and Jiuzhou Clinic dated October 27, 2009 (4)
- 10.23 Amendment to Voting Rights Proxy Agreement between Jiuxin Management and Jiuzhou Clinic dated October 27, 2009 (4)
- 10.24 Amendment to Consulting Services Agreement between Jiuxin Management and Jiuzhou Service dated October 27, 2009 (4)
- 10.25 Amendment to Operating Agreement between Jiuxin Management and Jiuzhou Service dated October 27, 2009 (4)
- 10.26 Amendment to Option Agreement between Jiuxin Management and Jiuzhou Service dated October 27, 2009 (4)
- 10.27 Amendment to Voting Rights Proxy Agreement between Jiuxin Management and Jiuzhou Service dated October 27, 2009 (4)
- 10.28 Director Offer Letter with Marc Thomas Serrio dated March 15, 2010 (6)
- 10.29 Indemnification Agreement with Marc Thomas Serrio dated March 15, 2010 (6)
- 10.30 Loanout Agreement with Worldwide Officers, Inc. dated May 14, 2010 (8)
- 10.31 Indemnification Agreement with Mr. Bennet Tchaikovsky dated May 14, 2010 (8)
- 10.32 Loanout Agreement with Worldwide Officers, Inc. dated August 1, 2011 (15)
- 10.33 Restricted Stock Award Agreement with Worldwide Officers, Inc. dated August 1, 2011 (15)
- 10.34 Employment Agreement with Mr. Ming Zhao dated August 1, 2011 (15)
- 10.35 Restricted Stock Award Agreement with Mr. Ming Zhao dated August 1, 2011 (15)
- 10.36 Director Offer Letter with Mr. Bennet Tchaikovsky dated August 1, 2011 (15)
- 10.37 Restricted Stock Award Agreement with Mr. Bennet Tchaikovsky dated August 1, 2011 (15)
- 14 Code of Business Conduct and Ethics (6)
- 16.1 Letter from Frazer Frost, LLP dated April 25, 2011 (12)
- 16.2 Letter from Frazer Frost, LLP dated May 19, 2011 (13)
- 21 List of subsidiaries (14)

- 31.1 Section 302 Certification by the Corporation's Chief Executive Officer *
- 31.2 Section 302 Certification by the Corporation's Chief Financial Officer *
- 32.1 Section 906 Certification by the Corporation's Chief Executive Officer *
- 32.2 Section 906 Certification by the Corporation's Chief Financial Officer *
- 99.1 Agreement for Logistics Services entered into between Jiuzhou Pharmacy and Zhejiang Yingte Logistics Co., Ltd. ("Yingte Logistics") dated January 1, 2011 (11)
- 99.2 Form of CFO Services Agreement entered into between Jiuzhou Pharmacy and Worldwide Officers, Inc. on July 30, 2009 (5)
- 99.3 Project Agreement between The People's Government of Qianhong Village, Lin'an, Zhejiang Province (the "Qianhong Local Government") and Jiuzhou Pharmacy dated February 27, 2010 (9)
- 99.4 Security Deposit Agreement between the Qianhong Local Government and Jiuzhou Pharmacy dated February 27, 2010 (9)

* Filed herewith

- (1) Incorporated by reference from the Registrant's Registration Statement on Form SB-2 filed on November 28, 2007
- (2) Incorporated by reference from the Registrant's Current Report on Form 8-K filed on July 15, 2008
- (3) Incorporated by reference from the Registrant's Current Report on Form 8-K filed on September 24, 2009
- (4) Incorporated by reference from the Registrant's Current Report on Form 8-K filed on October 30, 2009
- (5) Incorporated by reference from the Registrant's Registration Statement on Form S-1/A filed on January 27, 2010
- (6) Incorporated by reference from the Registrant's Current Report on Form 8-K filed on March 16, 2010
- (7) Incorporated by reference from the Registrant's Current Report on Form 8-K filed on April 14, 2010
- (8) Incorporated by reference from the Registrant's Current Report on Form 8-K filed on May 14, 2010
- (9) Incorporated by reference from the Registrant's Annual Report on Form 10-K filed on June 29, 2010
- (10) Incorporated by reference from the Registrant's Current Report on Form 8-K filed on November 3, 2010
- (11) Incorporated by reference from the Registrant's Quarterly Report on Form 10-Q filed on February 14, 2011
- (12) Incorporated by reference from the Registrant's Current Report on Form 8-K filed on April 25, 2011
- (13) Incorporated by reference from the Registrant's Current Report on Form 8-K filed on May 19, 2011
- (14) Incorporated by reference from the Registrant's Annual Report on Form 10-K filed on June 29, 2011
- (15) Incorporated by reference from the Registrant's Current Report on Form 8-K filed on August 2, 2011

SIGNATURES

In accordance with the requirements of the Exchange Act, the Registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

China Jo-Jo Drugstores, Inc.
(Registrant)

Date: August 15, 2011

By: /s/ Lei Liu
Lei Liu
Chief Executive Officer

Date: August 15, 2011

By: /s/ Ming Zhao
Ming Zhao
Chief Financial Officer