Taxation

Cayman Islands

Hutchison China MediTech Limited is incorporated in the Cayman Islands. The Cayman Islands currently levies no taxes on profits, income, gains or appreciation earned by individuals or corporations. In addition, our payment of dividends, if any, is not subject to withholding tax in the Cayman Islands. For more information, see Item 10.E. "Taxation—Overview of Tax Implications of Various Other Jurisdictions—Cayman Islands Taxation."

People's Republic of China

Our subsidiaries and joint ventures incorporated in the PRC are governed by the PRC EIT Law and regulations. Under the EIT Law, the standard EIT rate is 25% on taxable profits as reduced by available tax losses. Tax losses may be carried forward to offset any taxable profits for the following five years (ten years for those with HNTE status, with effective from 1 January 2018). Our subsidiary, Hutchison MediPharma, was granted the TASE status from January 1, 2010 to December 31, 2018, and has been successful in its application to renew its HNTE status from January 1, 2017 to December 31, 2019; whereas our non-consolidated joint ventures, Hutchison Baiyunshan and Shanghai Hutchison Pharmaceuticals, have been successful in their respective applications to renew their HNTE status from January 1, 2017 to December 31, 2019. Accordingly, these entities were subject to a preferential EIT rate of 15% for the years ended December 31, 2016, 2017 and 2018. Hutchison MediPharma (Suzhou) Limited, a wholly-owned subsidiary of Hutchison MediPharma, has successfully applied for the HNTE status in 2018 which will tentatively last three years from January 1, 2018 to December 31, 2020.

For more information, see Item 10.E. "Taxation—Taxation in the PRC." Please also see Item. 3 "Key Information—Risk Factors—Our business benefits from certain PRC government tax incentives. The expiration of, changes to, or our PRC subsidiaries/joint ventures failing to continuously meet the criteria for these incentives could have a material adverse effect on our operating results by significantly increasing our tax expenses."

Hong Kong

Hutchison China MediTech Limited and certain subsidiaries which have registered a branch in Hong Kong and are Hong Kong tax residents, as well as our subsidiaries incorporated in Hong Kong, are governed by applicable Hong Kong income tax laws and regulations. As such, they are subject to Hong Kong Profits Tax at the rate of 16.5% on their assessable profits as reduced by available tax losses for the years ended December 31, 2016, 2017 and 2018.

According to the EIT Law, dividends declared after January 1, 2008 and paid by PRC foreign-invested enterprises to their non-PRC parent companies will be subject to PRC withholding tax at 10% unless there is a tax treaty between the PRC and the jurisdiction in which the overseas parent company is a tax resident and which specifically exempts or reduces such withholding tax, and such tax exemption or reduction is approved by the relevant PRC tax authorities. Pursuant to the Arrangement, if the shareholder of the PRC enterprise is a Hong Kong tax resident and directly holds a 25% or more equity interest in the PRC enterprise and is considered to be the beneficial owner of dividends paid by the PRC enterprise, such withholding tax rate may be lowered to 5%, subject to approvals by the relevant PRC tax authorities. For more information, see Item 10.E. "Taxation—Taxation in the PRC" and "Taxation—Hong Kong Taxation."

Year Ended December 31, 2018 Compared to Year Ended December 31, 2017

Revenues

Our revenue decreased by 11.2% from $241.2 million for the year ended December 31, 2017 to $214.1 million for the year ended December 31, 2018, resulting from decreased revenue from our Commercial Platform.

Revenue from our Commercial Platform decreased by 15.8% from $205.2 million for the year ended December 31, 2017 to $172.9 million for the year ended December 31, 2018, primarily due to a decrease in revenue from our Prescription Drugs business. Revenue from our Prescription Drugs business decreased by 20.2% from $166.4 million for the year ended December 31, 2017 to $132.8 million for year ended December 31, 2018, primarily due to the implementation of the two-invoice system in China since October 2017. As a result, we started recording the service fees we earn from the distribution of certain third-party drugs instead of recording the gross sales of such products as we had done previously. The implementation of the two-invoice system has been a gradual and ongoing process in China, and we expect that the revenue from our Prescription Drugs business may experience further impact in the fiscal year 2019. Revenue from our Consumer Health business increased by 3.3% from $38.8 million for the year ended December 31, 2017 to $40.1 million for the year ended December 31, 2018, which was primarily attributable to increased sales of the Zhi Ling Tong infant nutrition and other health supplement products.

Revenue from our Innovation Platform increased by 14.5% from $36.0 million for the year ended December 31, 2017 to $41.2 million for the year ended December 31, 2018. The increase was attributable to a higher level of milestone payments that we received from our collaboration partners, including the milestone payment of $13.5 million that we received from Eli Lilly following the approval in September 2018 of fruquintinib capsules for drug registration in China for the treatment of metastatic colorectal cancer patients who have failed at least two prior systemic antineoplastic therapies, and $3.6 million from the sales and royalties of Elunate in China.

Our Commercial Platform's results of operations are affected by seasonality. For more information, see "—Factors Affecting our Results of Operations—Commercial Platform—Seasonality."

Cost of Sales

Our costs of sales decreased by 18.1% from $175.8 million for the year ended December 31, 2017 to $143.9 million for the year ended December 31, 2018. This decrease was in line with the decrease in our Commercial Platform revenue across these periods. Costs of sales as a percentage of our revenue from our Commercial Platform decreased from 85.7% to 82.4% across these periods due to the change to recording more services fees and to selling less lower margin third-party drugs.

Research and Development Expenses

Our research and development expenses increased by 51.2% from $75.5 million for the year ended December 31, 2017 to $114.2 million for the year ended December 31, 2018, which was primarily attributable to a $28.4 million increase in payments to CROs and other clinical trial related costs and an $10.5 million increase in employee compensation related costs. These increased costs incurred by our Innovation Platform were due to a significant expansion of clinical activities and rapid organizational growth to support such expansion. In particular, this increase was attributable to the expansion of the surufatinib, HMPL-523 and fruquintinib development programs. As a result, research and development expenses as a percentage of our revenue increased from 31.3% to 53.3% across these periods.

Selling Expenses

Our selling expenses decreased by 8.2% from $19.3 million for the year ended December 31, 2017 to $17.7 million for the year ended December 31, 2018. This decrease was primarily driven by a $3.0 million decrease in selling expenses under our Prescription Drugs business as the implementation of the two-invoice system caused us to start recording the costs associated with the service fees we earn from the distribution of certain third-party drugs as costs of sales instead of selling expenses as we had done previously. Selling expenses as a percentage of our revenue from our Commercial Platform increased slightly from 9.4% to 10.3% across these periods primarily due to the decrease in our Commercial Platform revenue.

Administrative Expenses

Our administrative expenses increased by 29.0% from $24.0 million for the year ended December 31, 2017 to $30.9 million for the year ended December 31, 2018. This increase was primarily due to a $3.0 million increase in administrative expenses incurred by our Innovation Platform, which mainly related to the increased staff cost to support the rapid expansion of our clinical activities and increased office expenses as we started to rent a new research and development facility in Shanghai in early 2018. Administrative expenses as a percentage of our revenue increased from 9.9% to 14.4% across these periods.

Other Income/Expenses

We had other expenses of $0.1 million for the year ended December 31, 2017, compared to other income of $6.0 million for the year ended December 31, 2018, primarily due to a higher level of interest income earned from the proceeds received from our follow-on offering in October 2017, which increased from $1.2 million for the year ended December 31, 2017 to $6.0 million for the year ended December 31, 2018. In addition, the increase in other income also resulted from the receipt of a new government grant by Hutchison Sinopharm as well as higher payments to us by the depositary bank which administers our ADS program in the year ended December 31, 2018 due to a higher number of our ADSs issued and eligible for compensation under the program.

Our interest expense decreased from $1.5 million for the year ended December 31, 2017 to $1.0 million for the year ended December 31, 2018, primarily due to a decrease in the guarantee fee payments on bank loans from $0.3 million in the year ended December 31, 2017 to nil in the year ended December 31, 2018.

Income Tax Expense

Our income tax expense increased by 28.7% from $3.1 million for the year ended December 31, 2017 to $4.0 million for the year ended December 31, 2018 primarily due to a higher level of taxable income from our Commercial Platform.

Equity in Earnings of Equity Investees

Our equity in earnings of equity investees, net of tax, decreased by 42.6% from $33.7 million for the year ended December 31, 2017 to $19.3 million for the year ended December 31, 2018. This decrease was primarily due to an increase in net loss at Nutrition Science Partners, our Innovation Platform's non-consolidated joint venture.

Shanghai Hutchison Pharmaceuticals

The following table shows a summary of the results of operations of Shanghai Hutchison Pharmaceuticals for the years indicated. The consolidated financial statements of Shanghai Hutchison

Pharmaceuticals are prepared in accordance with IFRS as issued by the IASB and are presented separately elsewhere in this annual report.

	Year Ended December 31,			
	2018		2017	
	($'000)	%	($'000)	%
Revenue	275,649	100.0	244,557	100.0
Cost of sales	(82,710)	(30.0)	(68,592)	(28.0)
Selling expenses	(111,984)	(40.6)	(104,504)	(42.7)
Administrative expenses	(14,522)	(5.3)	(13,257)	(5.4)
Taxation charge	(9,371)	(3.4)	(10,874)	(4.4)
Profit for the year	59,767	21.7	55,623	22.7
Equity in earnings of equity investee attributable to our company	29,884	10.8	27,812	11.4

Shanghai Hutchison Pharmaceuticals' revenue increased by 12.7% from $244.6 million for the year ended December 31, 2017 to $275.7 million for the year ended December 31, 2018, which was primarily due to increased sales of She Xiang Bao Xin pills, a vasodilator used in the treatment of heart conditions. Sales of She Xiang Bao Xin pills grew by 11.4% from $209.2 million for the year ended December 31, 2017 to $233.1 million for the year ended December 31, 2018, primarily due to continued price increases and geographical expansion of sales coverage. Additionally, other GSP product and service revenue increased by 27.6% from $18.1 million for the year ended December 31, 2017 to $23.1 million for the year ended December 31, 2018, primarily due to the higher provision of services from increased sales of Seroquel.

Cost of sales increased by 20.6% from $68.6 million for the year ended December 31, 2017 to $82.7 million for the year ended December 31, 2018, primarily due to increased cost of goods sold as a result of increased sales of She Xiang Bao Xin pills and the GSP product and service revenue.

Selling expenses during these periods increased by 7.2% from $104.5 million for the year ended December 31, 2017 to $112.0 million for the year ended December 31, 2018 as a result of increased spending on marketing and promotional activities to support the increase in sales.

Administrative expenses increased by 9.5% from $13.3 million for the year ended December 31, 2017 to $14.5 million for the year ended December 31, 2018 due to an increase in general overhead costs incurred.

Taxation charge decreased by 13.8% from $10.9 million for the year ended December 31, 2017 to $9.3 million for the year ended December 31, 2018, which was due to lower taxable profit primarily resulting from an increase of tax deductible research and development expenses of $0.4 million as well as the recognition of $0.7 million deferred tax assets on temporary differences arising from advertising and promotion expenditures incurred prior to 2018.

As a result of the foregoing, profit increased by 7.5% from $55.6 million for the year ended December 31, 2017 to $59.8 million for the year ended December 31, 2018. Our equity in earnings of equity investees contributed by this joint venture was $27.8 million and $29.9 million for the years ended December 31, 2017 and 2018, respectively.

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Hutchison Baiyunshan

The following table shows a summary of the results of operations of Hutchison Baiyunshan for the years indicated. The consolidated financial statements of Hutchison Baiyunshan are prepared in accordance with IFRS as issued by the IASB and are presented separately elsewhere in this annual report.

	Year Ended December 31,			
	2018		2017	
	($'000)	%	($'000)	%
Revenue	215,838	100.0	227,422	100.0
Cost of sales	(102,701)	(47.6)	(135,964)	(59.8)
Selling expenses	(70,501)	(32.7)	(45,262)	(19.9)
Administrative expenses	(25,997)	(12.0)	(24,541)	(10.8)
Taxation charge	(4,227)	(2.0)	(3,629)	(1.6)
Profit attributable to equity holders of Hutchison Baiyunshan	16,860	7.8	20,776	9.1
Equity in earnings of equity investee attributable to our company	8,430	3.9	10,388	4.6

Hutchison Baiyunshan's revenue decreased by 5.1% from $227.4 million for the year ended December 31, 2017 to $215.8 million for the year ended December 31, 2018 due to the divestment of one of its subsidiaries in September 2017, which was partially offset by a moderate to severe flu season and the elimination of manufacturing capacity constraints which increased sales of certain of its drug products in 2018.

Cost of sales decreased by 24.5% from $136.0 million for the year ended December 31, 2017 to $102.7 million for the year ended December 31, 2018, primarily due to the divestment of one of its subsidiaries in September 2017.

Selling expenses during these periods increased by 55.8% from $45.3 million for the year ended December 31, 2017 to $70.5 million for the year ended December 31, 2018 due to Hutchison Baiyunshan directly managing more marketing activities for its distributors to promote broader awareness and consistent messaging for Hutchison Baiyunshan's products.

Administrative expenses increased by 5.9% from $24.5 million for the year ended December 31, 2017 to $26.0 million for the year ended December 31, 2018 due to an increase in general overhead costs incurred.

Taxation charge increased by 16.5% from $3.6 million for the year ended December 31, 2017 to $4.2 million for the year ended December 31, 2018 which includes reductions to deferred tax assets of US$0.7 million for the year ended December 31, 2018 based on the likelihood of such asset being utilized in the near future.

As a result of the foregoing, profit attributable to equity holders of Hutchison Baiyunshan decreased by 18.8% from $20.8 million for the year ended December 31, 2017 to $16.9 million for the year ended December 31, 2018. Our equity in earnings of equity investees contributed by this joint venture was $10.4 million and $8.4 million for the years ended December 31, 2017 and 2018, respectively.

Nutrition Science Partners

The following table shows a summary of the results of operations of Nutrition Science Partners for the years indicated. The consolidated financial statements of Nutrition Science Partners are prepared in accordance with IFRS as issued by the IASB and are presented separately elsewhere in this annual report.

	Year Ended December 31,			
	2018		2017	
	($'000)	%	($'000)	%
Revenue	—	—	—	—
Loss for the year	(38,198)	100.0	(9,210)	100.0
Equity in earnings of equity investee attributable to our company	(19,099)	50.0	(4,605)	50.0

Nutrition Science Partners had losses of $9.2 million and $38.2 million for the years ended December 31, 2017 and 2018, respectively. Nutrition Science Partners had no revenue during these years. The increase in net loss across these periods was primarily attributable the full impairment provision recorded for its $30.0 million intangible asset related to in-progress research and development projects. Our equity in earnings of equity investees contributed by this joint venture were losses of $4.6 million and $19.1 million for the years ended December 31, 2017 and 2018, respectively.

For more information on the financial results of our non-consolidated joint ventures, see "—Key Components of Results of Operations—Equity in Earnings of Equity Investees."

Net Loss

As a result of the foregoing, our net loss increased from a net loss of $23.0 million for the year ended December 31, 2017 to a net loss of $71.3 million for the year ended December 31, 2018. Net loss attributable to our company increased from a net loss of $26.7 million for the year ended December 31, 2017 to a net loss of $74.8 million for the year ended December 31, 2018.

Operating Loss

Our operating loss increased from $18.4 million for the year ended December 31, 2017 to $66.3 million for the year ended December 31, 2018, as a result of a significant increase in the operating loss of our Innovation Platform from $52.0 million for the year ended December 31, 2017 to $102.6 million for the year ended December 31, 2018, partially offset by a slight increase in operating profit of our Commercial Platform from $45.1 million for the year ended December 31, 2017 to $47.0 million for the year ended December 31, 2018. The increase in the operating loss of our Innovation Platform across these periods was primarily due to a significant expansion of our clinical activities and an increase in the number of staff and other organizational growth to support such expansion.

Year Ended December 31, 2017 Compared to Year Ended December 31, 2016

Revenues

Our revenues increased by 11.6% from $216.1 million for the year ended December 31, 2016 to $241.2 million for the year ended December 31, 2017.

This increase was driven by a $24.4 million increase in revenue for the year ended December 31, 2017 from our Commercial Platform, representing a 13.5% increase from the revenue of $180.9 million for the year ended December 31, 2016. The consolidated revenue from our Prescription Drugs business increased by $16.6 million from $149.8 million for the year ended December 31, 2016 to $166.4 million for the year ended December 31, 2017. The increase was primarily attributable to the growth in our third-party drug distribution business. The consolidated revenue from our Consumer Health business also increased by

$7.8 million from $31.0 million for the year ended December 31, 2016 to $38.8 million for the year ended December 31, 2017. The increase was primarily attributable to higher levels of infant nutrition products and personal care products sold in 2017. The consolidated revenue from our Innovation Platform increased slightly by $0.8 million from $35.2 million for the year ended December 31, 2016 to $36.0 million for the year ended December 31, 2017. The increase was attributable to a higher level of service fees that we received from our joint ventures.

Our Commercial Platform's results of operations are affected by seasonality. For more information, see "—Factors Affecting our Results of Operations—Commercial Platform—Seasonality."

Cost of Sales

Our cost of sales increased by 12.5% from $156.3 million for the year ended December 31, 2016 to $175.8 million for the year ended December 31, 2017. This increase was primarily driven by a $15.4 million increase in cost of sales from Hutchison Sinopharm under our Prescription Drugs business, as well as a $4.0 million increase in cost of sales from Hutchison Hain Organic under our Consumer Health business. Cost of sales as a percentage of our revenue from our Commercial Platform decreased from 86.4% to 85.7% across these periods, primarily due to product mix resulting in an increased proportion of sales of higher margin products.

Research and Development Expenses

Our research and development expenses increased by 12.9% from $66.9 million for the year ended December 31, 2016 to $75.5 million for the year ended December 31, 2017, which was primarily attributable to a $5.5 million increase in payments to CROs and other clinical trial related costs and a $3.1 million increase in employee compensation related costs. These increased costs incurred by our Innovation Platform was due to a significant expansion of clinical activities and rapid organization growth to support these clinical activities. The number of ongoing clinical studies for our drug candidates increased from studies in 30 target patient populations as of December 31, 2016 to studies in 36 target patient populations as of December 31, 2017. In particular, this increase was attributable to the expansion of the savolitinib and fruquintinib development programs. As a result, research and development expenses as a percentage of our total revenue increased from 31.0% in the year ended December 31, 2016 to 31.3% in the year ended December 31, 2017.

Selling Expenses

Our selling expenses increased by 7.4% from $18.0 million for the year ended December 31, 2016 to $19.3 million for the year ended December 31, 2017. This increase was primarily driven by a $0.9 million increase in selling expenses under our Consumer Health business and a $0.4 million increase in selling expenses under our Prescription Drugs business. Selling expenses as a percentage of our revenue from our Commercial Platform decreased from 10.0% to 9.4% across these periods, primarily due to increased sales by our third-party Prescription Drug distribution and Consumer Health businesses.

Administrative Expenses

Our administrative expenses increased by 11.0% from $21.6 million for the year ended December 31, 2016 to $24.0 million for the year ended December 31, 2017. This increase was primarily due to a $1.2 million and $0.9 million increase in administrative expenses incurred by our Innovation Platform and corporate head office, mainly related to the increased staff cost, office expenses and organization and third-party advisor costs as a result of operating as a U.S. public company for a full calendar year. Administrative expenses had remained relatively stable as a percentage of our total revenue.

Other Expenses

Total other expenses decreased from $0.7 million for the year ended December 31, 2016 to $0.1 million for the year ended December 31, 2017, primarily due to higher interest income offset by higher foreign currency translation loss.

Our interest income increased from $0.5 million for the year ended December 31, 2016 to $1.2 million for the year ended December 31, 2017. The increase was attributable to a higher level of bank deposits after receiving proceeds from our follow-on offering in October 2017. Our interest expense decreased slightly from $1.6 million for the year ended December 31, 2016 to $1.5 million for the year ended December 31, 2017. These interest expenses primarily comprised interest and guarantee fee payments on bank loans in 2016 and 2017.

Income Tax Expense

Our income tax expense decreased by 28.9% from $4.3 million for the year ended December 31, 2016 to $3.1 million for the year ended December 31, 2017 due to a decrease in withholding taxes accrued on the net income from our Commercial Platform businesses for the year ended December 31, 2017. The higher withholding tax accrued for the year ended December 31, 2016 was due to equity in earnings of Shanghai Hutchison Pharmaceuticals including a one-time gain of $40.4 million relating to land compensation and other government subsidies.

Equity in Earnings of Equity Investees

Our equity in earnings of equity investees, net of tax, decreased by 49.2% from $66.2 million for the year ended December 31, 2016 to $33.7 million for the year ended December 31, 2017. This decrease was primarily due to a decrease in net income at our Commercial Platform's non-consolidated joint ventures as well as an increase in net loss at Nutrition Science Partners, our Innovation Platform's non-consolidated joint venture. Our equity in earnings of Shanghai Hutchison Pharmaceuticals included one-time gains, net of tax, of $40.4 million from land compensation and other government subsidies in the year ended December 31, 2016 and $2.5 million from government subsidies in the year ended December 31, 2017 in each case paid to Shanghai Hutchison Pharmaceuticals by the Shanghai government.

Shanghai Hutchison Pharmaceuticals

The following table shows a summary of the results of operations of Shanghai Hutchison Pharmaceuticals for the years indicated. The consolidated financial statements of Shanghai Hutchison Pharmaceuticals are prepared in accordance with IFRS as issued by the IASB and are presented separately elsewhere in this annual report.

	Year Ended December 31,			
	2017		2016	
	($'000)	%	($'000)	%
Revenue	244,557	100.0	222,368	100.0
Cost of sales	(68,592)	(28.0)	(64,237)	(28.9)
Selling expenses	(104,504)	(42.7)	(92,487)	(41.6)
Administrative expenses	(13,257)	(5.4)	(13,278)	(6.0)
Gain on disposal of assets held for sale	—	—	88,536	39.8
Taxation charge	(10,874)	(4.4)	(27,645)	(12.4)
Profit for the year	55,623	22.7	120,499	54.2
Equity in earnings of equity investee attributable to our company	27,812	11.4	60,250	27.1

Shanghai Hutchison Pharmaceuticals' revenue increased by 10.0% from $222.4 million for the year ended December 31, 2016 to $244.6 million for the year ended December 31, 2017, which was primarily due to increased sales of She Xiang Bao Xin pills, a vasodilator used in the treatment of heart conditions. Sales of She Xiang Bao Xin pills grew by 7.1% from $195.4 million for the year ended December 31, 2016 to $209.2 million for the year ended December 31, 2017, primarily due to continued price increases and geographical expansion of sales coverage.

Cost of sales increased by 6.8% from $64.2 million for the year ended December 31, 2016 to $68.6 million for the year ended December 31, 2017, primarily due to increased cost of goods sold as a result of increased sales of She Xiang Bao Xin pills.

Selling expenses during these periods increased by 13.0% from $92.5 million for the year ended December 31, 2016 to $104.5 million for the year ended December 31, 2017 as a result of increased spending on marketing and promotional activities to support the increase in sales.

Administrative expenses remained relatively stable at $13.3 million for the years ended December 31, 2016 and 2017.

Taxation charge decreased by 60.7% from $27.6 million for the year ended December 31, 2016 to $10.9 million for the year ended December 31, 2017, which was primarily due to the decrease in profit before taxation between these periods.

As a result of the foregoing and the one-time gain of $40.4 million from land compensation and other government subsidies received from the Shanghai government in 2016 which did not occur in 2017, profit decreased by 53.8% from $120.5 million for the year ended December 31, 2016 to $55.6 million for the year ended December 31, 2017. Our equity in earnings of equity investees contributed by this joint venture was $60.3 million and $27.8 million for the years ended December 31, 2016 and 2017, respectively.

Hutchison Baiyunshan

The following table shows a summary of the results of operations of Hutchison Baiyunshan for the years indicated. The consolidated financial statements of Hutchison Baiyunshan are prepared in accordance with IFRS as issued by the IASB and are presented separately elsewhere in this annual report.

	Year Ended December 31,			
	2017		2016	
	($'000)	%	($'000)	%
Revenue	227,422	100.0	224,131	100.0
Cost of sales	(135,964)	(59.8)	(134,776)	(60.1)
Selling expenses	(45,262)	(19.9)	(46,873)	(20.9)
Administrative expenses	(24,541)	(10.8)	(21,716)	(9.7)
Taxation charge	(3,629)	(1.6)	(3,631)	(1.6)
Profit attributable to equity holders of Hutchison Baiyunshan	20,776	9.1	20,376	9.1
Equity in earnings of equity investee attributable to our company	10,388	4.6	10,188	4.5

Hutchison Baiyunshan's revenue increased slightly by 1.5% from $224.1 million for the year ended December 31, 2016 to $227.4 million for the year ended December 31, 2017, which was primarily due to increased sales of certain of its drug products.

Cost of sales increased by 0.9% from $134.8 million for the year ended December 31, 2016 to $136.0 million for the year ended December 31, 2017, primarily due to increased sales. The increase in cost of sales was smaller than the increase in revenues due to a change in product mix resulting in a higher proportion of sales of higher margin products.

Selling expenses during these periods decreased by 3.4% from $46.9 million for the year ended December 31, 2016 to $45.3 million for the year ended December 31, 2017 due to less sales and marketing activities.

Administrative expenses increased by 13.0% from $21.7 million for the year ended December 31, 2016 to $24.5 million for the year ended December 31, 2017 due to an increase in general overhead costs incurred.

Taxation charge remained relatively stable at $3.6 million for the years ended December 31, 2016 and 2017 due to relatively stable profit before taxation across these periods.

As a result of the foregoing, profit attributable to equity holders of Hutchison Baiyunshan increased by 2.0% from $20.4 million for the year ended December 31, 2016 to $20.8 million for the year ended December 31, 2017. Our equity in earnings of equity investees contributed by this joint venture was $10.2 million and $10.4 million for the years ended December 31, 2016 and 2017, respectively.

Nutrition Science Partners

The following table shows a summary of the results of operations of Nutrition Science Partners for the years indicated. The consolidated financial statements of Nutrition Science Partners are prepared in accordance with IFRS as issued by the IASB and are presented separately elsewhere in this annual report.

	Year Ended December 31,			
	2017		2016	
	($'000)	%	($'000)	%
Revenue	—	—	—	—
Loss for the year	(9,210)	100.0	(8,482)	100.0
Equity in earnings of equity investee attributable to our company	(4,605)	50.0	(4,241)	50.0

Nutrition Science Partners had losses of $8.5 million and $9.2 million for the years ended December 31, 2016 and 2017, respectively. Nutrition Science Partners had no revenue during these periods. The increase in net loss across these periods was primarily attributable to higher expenditures on personnel costs related to the development of drug candidates from Nutrition Science Partners' botanical library. Our equity in earnings of equity investees contributed by this joint venture was losses of $4.2 million and $4.6 million for the years ended December 31, 2016 and 2017, respectively.

For more information on the financial results of our non-consolidated joint ventures, see "—Key Components of Results of Operations—Equity in Earnings of Equity Investees."

Net (Loss)/Income

As a result of the foregoing, our net income decreased from a net income of $14.6 million for the year ended December 31, 2016 to a net loss of $23.0 million for the year ended December 31, 2017. Net income attributable to our company decreased from a net income of $11.7 million for the year ended December 31, 2016 to a net loss of $26.7 million for the year ended December 31, 2017.

Operating Profit/(Loss)

Our operating profit decreased from an operating profit of $20.5 million for the year ended December 31, 2016 to an operating loss of $18.4 million for the year ended December 31, 2017 as a result of a significant decrease in operating profit of our Commercial Platform from $74.3 million for the year ended December 31, 2016 to $45.1 million for the year ended December 31, 2017 as well as an increase in operating loss of our Innovative Platform from $40.8 million for the year ended December 31, 2016 to $52.0 million for the year ended December 31, 2017. The decrease in operating profit of our Commercial

Platform across these periods was primarily due to equity in earnings of Shanghai Hutchison Pharmaceuticals including a one-time gain of $40.4 million relating to land compensation and other government subsidies in 2016 which did not occur in 2017. The increase in operating loss of our Innovation Platform was due to a significant expansion of clinical activities, rapid organization growth to support these clinical activities and investment in the expansion of small molecule manufacturing operations.

B. Liquidity and Capital Resources

To date, we have taken a multi-source approach to fund our operations, including through cash flows generated and dividend payments from our Commercial Platform, service and milestone and upfront payments from our Innovation Platform's collaboration partners, and bank borrowings. Since our founding, we have received various financial support from CK Hutchison in the form of undertakings for bank borrowings, as well as investments from other third parties, proceeds from our listings on the AIM market of the London Stock Exchange in 2006 and the Nasdaq Global Select Market in 2016 and our follow-on offering in 2017.

Our Innovation Platform has historically not generated significant profits or has operated at a net loss, as creating potential global first-in-class or best-in-class drug candidates requires a significant investment of resources over a prolonged period of time. As a result, we anticipate that we may need additional financing for our Innovation Platform in future periods. See Item 3.D. "Risk Factors—Risks Related to Our Innovation Platform—Historically, our Innovation Platform has not generated significant profits or has operated at a net loss, and our future profitability is dependent on the successful commercialization of our drug candidates, including fruquintinib which received approval from the National Medical Products Administration of China, or NMPA (formerly known as the China Food and Drug Administration), in September 2018."

As of December 31, 2018, we had cash and cash equivalents and short-term investments of $301.0 million and unutilized bank facilities of $119.3 million. Substantially all of our bank deposits are at major financial institutions, which we believe are of high credit quality. As of December 31, 2018, we had $26.7 million in bank loans, all of which was related to a term loan from Scotiabank. The total weighted average cost of bank borrowings for the year ended December 31, 2018 was 2.8% per annum. We incurred no guarantee fees for the year ended December 31, 2018. For additional information, see "—Loan Facilities."

Certain of our subsidiaries and non-consolidated joint ventures, including those registered as wholly foreign-owned enterprises in China, are required to set aside at least 10.0% of their after-tax profits to their general reserves until such reserves reach 50.0% of their registered capital. There is no fixed percentage of after-tax profit required to be set aside for the general reserves for our PRC joint ventures. Profit appropriated to the reserve funds for our subsidiaries and non-consolidated joint ventures incorporated in the PRC was approximately $15,000, $10,000 and $15,000 for the years ended December 31, 2016, 2017 and 2018, respectively. In addition, as a result of PRC regulations restricting dividend distributions from such reserve funds and from a company's registered capital, our PRC subsidiaries are restricted in their ability to transfer a certain amount of their net assets to us as cash dividends, loans or advances. This restricted portion amounted to $7.4 million as of December 31, 2018. Although we do not currently require any such dividends, loans or advances from our PRC subsidiaries to fund our operations, should we require additional sources of liquidity in the future, such restrictions may have a material adverse effect on our liquidity and capital resources. For more information, see Item 4.B. "Business Overview—Regulation—PRC Regulation of Foreign Currency Exchange, Offshore Investment and State-Owned Assets—Regulation on Dividend Distribution."

In addition, our non-consolidated joint ventures held an aggregate of $59.2 million in cash and cash equivalents and no bank borrowings as of December 31, 2018. These cash and cash equivalents are only accessible by us through dividend payments from these joint ventures. The level of dividends declared by these joint ventures is subject to agreement each year between us and our joint venture partners based on the profitability and working capital needs of the joint ventures. As a result, we cannot guarantee that these joint ventures will continue to pay dividends to us in the future at the same rate we have enjoyed in the past, or at all, which may have a material adverse effect on our liquidity and capital resources. As of December 31, 2018, our Innovation Platform joint venture, Nutrition Science Partners, has not paid any dividends. For more information, see Item 3.D. "Risk Factors—Risks Related to Our Commercial Platform—As a significant portion of our Commercial Platform business is conducted through joint ventures, we are largely dependent on the success of our joint ventures and our receipt of dividends or other payments from our joint ventures for cash to fund our operations."

We believe that our current levels of cash and cash equivalents, short-term investments, along with cash flows from operations, dividend payments and bank borrowings, will be sufficient to meet our anticipated cash needs for at least the next 12 months. However, we may require additional financing in order to fund all of the clinical development efforts at our Innovation Platform that we plan to undertake to accelerate the development of our clinical-stage drug candidates. For more information, see Item 3.D. "Risk Factors—Risks Related to Our Financial Position and Need for Capital."

	Year Ended December 31,		
	2018	2017	2016
		($'000)	
Cash Flow Data:			
Net cash used in operating activities	(32,847)	(8,943)	(9,569)
Net cash generated from/(used in) investing activities	43,752	(260,780)	(33,597)
Net cash (used in)/generated from financing activities	(8,231)	273,196	92,435
Net increase in cash and cash equivalents	2,674	3,473	49,269
Effect of exchange rate changes	(1,903)	2,361	(1,779)
Cash and cash equivalents at beginning of the year	85,265	79,431	31,941
Cash and cash equivalents at end of the year	86,036	85,265	79,431

Net Cash used in Operating Activities

Net cash used in operating activities was $8.9 million for the year ended December 31, 2017 compared to net cash used in operating activities of $32.8 million for the year ended December 31, 2018. The net change of $23.9 million was primarily attributable to the increase in net loss of $48.3 million from $23.0 million for the year ended December 31, 2017 to $71.3 million for the year ended December 31, 2018 which included our company's $15.0 million share of Nutrition Science Partner's non-cash impairment provision. See Item 4.B. "Business Overview—Overview of Our Collaborations—Nestlé Health Science" for more details relating to this impairment provision. Additionally, the net change was also a result of a decrease in dividends received from equity investees of $20.4 million from $55.6 million for the year ended December 31, 2017 to $35.2 million for the year ended December 31, 2018, which resulted from the relatively high level of dividends received from our non-consolidated joint venture Shanghai Hutchison Pharmaceuticals in the year ended December 31, 2017 following the one-time land compensation that it received from the Shanghai government. The net change was partially offset by the effects of changes in working capital. In particular, there was a $16.3 million increase in other payables, accruals and advance receipts for the year ended December 31, 2018, as compared to $5.2 million increase for the year ended December 31, 2017, and a $1.3 million increase in accounts payable for the year ended December 31, 2018, as compared to a $11.2 million decrease for the year ended December 31, 2017.

Net cash used in operating activities was $9.6 million for the year ended December 31, 2016 compared to net cash used in operating activities of $8.9 million for the year ended December 31, 2017. The net change was primarily attributable to a $25.1 million increase in dividends received from our equity investees from $30.5 million for the year ended December 31, 2016 to $55.6 million for the year ended December 31, 2017 which was the result of increased revenue and funds available from land compensation paid to our equity investees in 2016. This increase was partially offset by an increase in research and development spending in our Innovation Platform as well as the effects of changes in working capital, namely an aggregate decrease of $14.5 million in the year ended December 31, 2017 primarily due to delayed payments from 2016 which were settled in 2017, as compared to an aggregate increase of $3.4 million in the year ended December 31, 2016.

Net Cash generated from/(used in) Investing Activities

Net cash used in investing activities was $260.8 million for the year ended December 31, 2017, compared to net cash generated from investing activities of $43.8 million for the year ended December 31, 2018. The net change of $304.6 million was primarily attributable to the net deposits into short-term investments of $248.8 million for the year ended December 31, 2017 compared to net withdrawal of deposits in short-term investments of $58.1 million for the year ended December 31, 2018.

Net cash used in investing activities was $33.6 million for the year ended December 31, 2016, compared to net cash used in investing activities of $260.8 million for the year ended December 31, 2017. This change was primarily attributable to net deposits in short-term investments of $248.8 million for the year ended December 31, 2017 compared to $24.3 million for the year ended December 31, 2016. This change was also attributable to an additional $7.0 million share capital contribution to Nutrition Science Partners in 2017 compared to $5.0 million in 2016.

Net Cash (used in)/generated from Financing Activities

Net cash generated from financing activities was $273.2 million for the year ended December 31, 2017, compared to net cash used in financing activities of $8.2 million for the year ended December 31, 2018. The net change of $281.4 million was primarily attributable to net proceeds of $292.7 million from the issuance of ordinary shares in the form of ADSs upon our follow-on offering in the Unites States in October 2017 as well as a net repayment of bank borrowings of $16.9 million in the year ended December 31, 2017 as compared to a net repayment of bank borrowings of $3.1 million in the year ended December 31, 2018.

Net cash generated from financing activities was $92.4 million for the year ended December 31, 2016, compared to net cash generated from financing activities of $273.2 million for the year ended December 31, 2017. This change was primarily attributable to net proceeds of $292.7 million from the issuance of ordinary shares in the form of ADS upon our follow-on offering in the United States in October 2017 as compared to net proceeds of $97.3 million from the issuance of ordinary shares in the form of ADS upon our initial public offering in the United States in 2016. The change was also attributable to a net decrease in bank borrowings of $16.9 million for the year ended December 31, 2017 as compared to a net decrease of $3.1 million for the year ended December 31, 2016.

Loan Facilities

In November 2015, we renewed a three-year revolving loan facility with HSBC with an annual interest rate of 1.25% over the Hong Kong Inter-bank Offered Rate, or HIBOR. In February 2017, $2.6 million was drawn from this facility, and the amount was fully repaid in March 2017. Upon maturity in November 2018, we further renewed this revolving loan facility for an additional three years to November 2021. The facility amount of this loan is HK$234.0 million ($30.0 million) with an annual interest rate of 0.85% over HIBOR. No amount was drawn from this loan facility as December 31, 2018.

In February 2017, our subsidiary Hutchison China MediTech (HK) Limited entered into two credit facility agreements with each of Bank of America N.A. and Deutsche Bank AG for the provision of unsecured credit facilities in the aggregate amount of HK$546.0 million ($70.0 million). The credit facility with Bank of America N.A. included (i) a HK$156.0 million ($20.0 million) term loan facility and (ii) a HK$195.0 million ($25.0 million) revolving loan facility, both with a term of 18 months and an annual interest rate of 1.25% over HIBOR. The term loan was drawn from this credit facility in March 2017 and repaid and terminated in May 2018. The credit facility with Deutsche Bank AG included (i) a HK$78.0 million ($10.0 million) term loan facility and (ii) a HK$117.0 million ($15.0 million) revolving loan facility, both with a term of 18 months and an annual interest rate of 1.25% over HIBOR. The term loan was drawn from this credit facility in August 2017 and repaid and terminated in May 2018. Both revolving loan facilities were terminated in August 2018.

In August 2018, our subsidiary Hutchison China MediTech (HK) Limited entered into new credit facility agreements with each of Bank of America N.A. and Deutsche Bank AG for the provision of unsecured credit facilities in the aggregate amount of HK$507.0 million ($65.0 million). The credit facility with Bank of America N.A. is a HK$351.0 million ($45.0 million) revolving loan facility, with a term of 24 months and an annual interest rate of 1.35% over HIBOR. The credit facility with Deutsche Bank AG is a HK$156.0 million ($20.0 million) revolving loan facility with a term of 24 months and an annual interest rate of 1.35% over HIBOR. These credit facilities are guaranteed by us and include certain financial covenant requirements. As of December 31, 2018, no amount was drawn from either of these two revolving loan facilities.

In November 2017, our subsidiary Hutchison China MediTech Finance Holdings Limited entered into a HK$210.0 million ($26.9 million) three-year term loan and HK$190.0 million ($24.4 million) 18-month revolving loan facility with Scotiabank. The term loan facility bears an annual interest rate of 1.50% over HIBOR and the revolving loan facility bears an annual interest rate of 1.25% over HIBOR. The term loan and revolving loan facility will expire in November 2020 and May 2019, respectively. As of December 31, 2018, $26.9 million was drawn from the term loan. Our previous four-year term loan with Scotiabank entered in June 2014 was fully repaid in November 2017. The previous term loan was guaranteed by Hutchison Whampoa Limited, a wholly owned subsidiary of CK Hutchison, for an annual guarantee fee of 1.75%. The new term loan with Scotiabank entered into in November 2017 is not guaranteed by Hutchison Whampoa Limited.

Our non-consolidated joint ventures Shanghai Hutchison Pharmaceuticals, Hutchison Baiyunshan and Nutrition Science Partners had no bank borrowings outstanding as of December 31, 2018.

Capital Expenditures

We had capital expenditures of $4.3 million, $5.0 million and $6.4 million for the years ended December 31, 2016, 2017 and 2018, respectively. Our capital expenditures during these periods were primarily used for the purchases of property, plant and equipment to expand the Hutchison MediPharma research facilities and the new manufacturing facility in Suzhou, China, which produces Elunate and other clinical supplies. Our capital expenditures have been primarily funded by cash flows from operations and proceeds from our initial public and follow-on offering in the United States.

As of December 31, 2018, we had commitments for capital expenditures of approximately $1.5 million, primarily for purchases of property, plant and equipment to expand the Hutchison MediPharma research facilities and the new Suzhou manufacturing facility. We expect to fund these capital expenditures through cash flows from operations and existing cash resources.

Our non-consolidated joint venture Shanghai Hutchison Pharmaceuticals had capital expenditures (net of government subsidies) of $11.0 million, $6.2 million and $5.2 million for the years ended December 31, 2016, 2017 and 2018, respectively. These capital expenditures were primarily related to the construction and improvements of the production facilities in Feng Pu district in Shanghai. These capital expenditures were primarily funded through cash flows from operations of Shanghai Hutchison Pharmaceuticals and bank borrowings.

Our non-consolidated joint venture Hutchison Baiyunshan had capital expenditures of $13.2 million, $7.2 million and $5.4 million for the years ended December 31, 2016, 2017 and 2018, respectively. These capital expenditures were primarily related to the construction and improvements of the production facilities in Bozhou and an office building in Guangzhou. These capital expenditures were primarily funded through cash flows from operations of Hutchison Baiyunshan.

C. Research and Development, Patents and Licenses, etc.

Full details of our research and development activities and expenditures are given in the "Business" and "Operating and Financial Review and Prospects" sections of this annual report above.

D. Trend Information.

Other than as described elsewhere in this annual report, we are not aware of any trends, uncertainties, demands, commitments or events that are reasonably likely to have a material adverse effect on our revenue, income, profitability, liquidity or capital resources, or that would cause our reported financial information not necessarily to be indicative of future operation results or financial condition.

E. Off-balance Sheet Arrangements.

Other than some of the operating lease obligations set forth in the table below, we did not have during the periods presented, and we do not currently have, any off-balance sheet arrangements as defined under the rules of the SEC.

F. Tabular Disclosure of Contractual Obligations.

The following table sets forth our contractual obligations as of December 31, 2018. Our purchase obligations relate to property, plant and equipment that are contracted for but not yet paid. Our operating lease obligations primarily comprise future aggregate minimum lease payments in respect of various factories and offices under non-cancellable operating lease agreements.

	Payment Due by Period				
	Total	Less Than 1 Year	1-3 Years	3-5 Years	More Than 5 Years
			($'000)		
Bank borrowings	26,923	—	26,923	—	—
Interest on bank borrowings	1,225	641	584	—	—
Purchase obligations	1,498	1,498	—	—	—
Operating lease obligations	8,835	3,026	3,791	1,692	326
Total	38,481	5,165	31,298	1,692	326

Shanghai Hutchison Pharmaceuticals

The following table sets forth the contractual obligations of our non-consolidated joint venture Shanghai Hutchison Pharmaceuticals as of December 31, 2018. Shanghai Hutchison Pharmaceuticals' purchase obligations comprise capital commitments for property, plant and equipment contracted for but not yet paid. Shanghai Hutchison Pharmaceuticals' operating lease obligations primarily comprise future aggregate minimum lease payments in respect of various offices under non-cancellable operating lease agreements.

	Payment Due by Period				
	Total	Less Than 1 Year	1-3 Years	3-5 Years	More Than 5 Years
			($'000)		
Purchase obligations	579	579	—	—	—
Operating lease obligations	1,241	610	619	12	—
Total	1,820	1,189	619	12	—

Hutchison Baiyunshan

The following table sets forth the contractual obligations of our non-consolidated joint venture Hutchison Baiyunshan as of December 31, 2018. Hutchison Baiyunshan's purchase obligations comprise capital commitments for property, plant and equipment contracted for but not yet paid. Hutchison Baiyunshan's finance and operating lease obligations primarily comprise future aggregate minimum lease payments in respect of various warehouses under non-cancellable lease agreements.

	Payment Due by Period				
	Total	Less Than 1 Year	1-3 Years	3-5 Years	More Than 5 Years
			($'000)		
Purchase obligations	780	780	—	—	—
Finance lease obligations	372	105	227	40	—
Operating lease obligations	1,232	885	295	52	—
Total	2,384	1,770	522	92	—

Quantitative and Qualitative Disclosures About Market Risk

Foreign Exchange Risk

Substantially all of our revenue and expenses are denominated in renminbi, and our financial statements are presented in U.S. dollars. We do not believe that we currently have any significant direct foreign exchange risk and have not used any derivative financial instruments to hedge our exposure to such risk. Although, in general, our exposure to foreign exchange risks should be limited, the value of your investment in our ADSs will be affected by the exchange rate between the U.S. dollar and the renminbi because the value of our business is effectively denominated in renminbi, while the ADSs will be traded in U.S. dollars.

The value of the renminbi against the U.S. dollar and other currencies may fluctuate and is affected by, among other things, changes in China's political and economic conditions. The conversion of renminbi into foreign currencies, including U.S. dollars, has been based on rates set by the PBOC. On July 21, 2005, the PRC government changed its decade-old policy of pegging the value of the renminbi to the U.S. dollar. Under the revised policy, the renminbi is permitted to fluctuate within a narrow and managed band against a basket of certain foreign currencies. This change in policy resulted in a more than 20% appreciation of the renminbi against the U.S. dollar in the following three years. Between July 2008 and June 2010, this appreciation halted, and the exchange rate between the renminbi and U.S. dollar remained within a narrow band. In June 2010, the PBOC announced that the PRC government would increase the flexibility of the exchange rate, and thereafter allowed the renminbi to appreciate slowly against the U.S. dollar within the narrow band fixed by the PBOC. However, more recently, the PBOC has significantly devalued the renminbi against the U.S. dollar. If we decide to convert renminbi into U.S. dollars for the purpose of making payments for dividends on our ordinary shares or ADSs or for other business purposes, appreciation of the U.S. dollar against the renminbi would have a negative effect on the U.S. dollar amounts available to us.

Credit Risk

Substantially all of our bank deposits are in major financial institutions, which we believe are of high credit quality. We limit the amount of credit exposure to any single financial institution. We make periodic assessments of the recoverability of trade and other receivables and amounts due from related parties. Our historical experience in collection of receivables falls within the recorded allowances, and we believe that we have made adequate provision for uncollectible receivables.

Interest Rate Risk

We have no significant interest-bearing assets except for bank deposits. Our exposure to changes in interest rates is mainly attributable to our bank borrowings, which bear interest at floating interest rates and expose us to cash flow interest rate risk. We have not used any interest rate swaps to hedge our exposure to interest rate risk. We have performed sensitivity analysis for the effects on our results for the year from changes in interest rates on floating rate borrowings. The sensitivity to interest rates used is based on the market forecasts available at the end of the reporting period and under the economic environments in which we operate, with other variables held constant. According to the analysis, the impact on our net loss of a 1.0% interest rate shift would be a maximum increase/decrease of $0.3 million for the year ended December 31, 2018.

Inflation

In recent years, China has not experienced significant inflation, and thus inflation has not had a material impact on our results of operations. According to the National Bureau of Statistics of China, the Consumer Price Index in China increased by 2.0%, 1.8% and 1.9% in 2016, 2017 and 2018, respectively. Although we have not been materially affected by inflation in the past, we can provide no assurance that we will not be affected in the future by higher rates of inflation in China.

Recently Issued Accounting Standards

In May 2014, the Financial Accounting Standards Board, or FASB, issued ASU 2014-09, Revenue from Contracts with Customers (Topic 606), or ASU 2014-09, to clarify the principles of recognizing revenue and create common revenue recognition guidance for U.S. GAAP and International Financial Reporting Standards. An entity has the option to apply the provisions of ASU 2014-09 either retrospectively to each prior reporting period presented or retrospectively with the cumulative effect of initially applying this standard recognized at the date of initial application. ASU 2014-09 is effective for fiscal years and interim periods within those years beginning after December 15, 2017, and early adoption is permitted but not earlier than the original effective date of December 15, 2016. The new standard supersedes U.S. GAAP guidance on revenue recognition and requires the use of more estimates, judgments and additional disclosures.

We adopted the new standard using the modified retrospective method on January 1, 2018 and have assessed the impact on revenue from customers. Our revenue from contracts with customers comprises of research and development projects in our Innovation Platform and sales of goods and services in our Commercial Platform operating segments. The changes from applying the new guidance primarily impacted the Innovation Platform.

Innovation Platform—We have reviewed our research and development contracts and identified two contracts related to our license and collaboration arrangements that will be impacted by the application of ASU 2014-09. The license and collaboration arrangements contain multiple performance obligations:

(1) the license to the drug compound; and (2) the research and development services for each specified treatment indication. The transaction price includes fixed and variable consideration in the form of upfront payment, research and development costs reimbursements, contingent milestone payments and sales-based royalties. The allocation of the transaction price to each performance obligation is based on the relative standalone selling price of each performance obligation. We have determined that control of the license to the drug compound was transferred as of the inception date of the collaboration agreements and consequently, amounts allocated to this performance obligation are recognized at a point in time. Conversely, control of the research and development services for each specified indication is transferred over time and amounts allocated to these performance obligations are recognized over time using cost inputs as a measure of progress. In addition, royalty revenues will be recognized as future sales occur as they meet the requirements for the sales-usage based royalty exception. We recorded a US$1.1 million deferral of revenue as a cumulative adjustment to opening accumulated loss upon adoption.

Commercial Platform—For sales of goods and services, we have applied a portfolio approach to aggregate contracts into portfolios whose performance obligations do not differ materially from each other. In our assessment of each portfolio, we have assessed the contracts under the new five-step model and do not expect a significant impact to the timing or amount of revenue recognition under the new guidance. Control of the goods passes to the customer when the goods are delivered, which matches the timing of revenue recognition under the our existing accounting policy.

We have applied updates to the new guidance in our assessment including ASU 2016-08, Principal versus Agent Considerations, ASU 2016-10, Identifying Performance Obligations and Licensing.

In February 2016, the Financial Accounting Standards Board, or FASB, issued ASU 2016-02, Leases (Topic 842), or ASU 2016-02. The core principle of ASU 2016-02 is that a lessee should recognize the assets and liabilities that arise from leases. A lessee should recognize on the balance sheet a liability to make lease payments (the lease liability) and a right of use asset representing its right to use the underlying asset for the lease term. We elected the short-term lease exception to not recognize right-of-use assets and lease liabilities for leases with a term of 12 months or less and will recognize lease expense for such leases generally on a straight line basis over the lease term. ASU 2016-02 is effective for fiscal years and interim periods within those years beginning after December 15, 2018. We adopted the new standard using the optional transition method (from ASU 2018-11, Leases Targeted Improvements) on January 1, 2019. A gross up to the consolidated balance sheet was recognized on the date of adoption of US$5.7 million and US$6.4 million in right-of-use assets and lease liabilities respectively, primarily related to our various factories and offices under non-cancellable lease agreements that were accounted as operating leases under ASC 840, Leases (Topic 840) as at December 31, 2018. Additionally, we do not expect a significant impact to the consolidated statements of operations after the adoption of ASC 842 as the pattern of expense recognition should not change materially for such operating leases.

Other amendments that have been issued 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 our consolidated financial statements upon adoption.