MANAGEMENT DISCUSSION SECTION

Operator: Welcome to the Chindex International Third Quarter Fiscal 2010 Conference Call. This call is being recorded. I will now turn the call over to your host to Roberta Lipson, the CEO; and Larry Pemble, the CFO of Chindex. Please go ahead.

Roberta Lipson, Chief Executive Officer and President

Good morning. I'd like to welcome you all to our conference call to discuss Chindex International's third quarter versus for the fiscal year 2010. As in the past, we have pre-recorded our initial comments, which will be followed by a live Q&A session. Joining me today on the call is Larry Pemble, our CFO.

Before we proceed with a summary of operating results for the period and an update on recent events, I'll ask Larry to read the Safe Harbor statement. I'll make some brief comments and then Larry will do the quarterly financial results and our outlook for the year. I'll then comment on the business environment and then we will return to Q&A.

Larry, will you proceed with the Safe Harbor statement please?

Lawrence Pemble, Executive Vice President and Chief Financial Officer

Yes, thank you, Roberta, and good morning, everyone. Statements made in this conference call relating to plans, strategies, objectives, economic performance and trends and other statements that are not descriptions of historical facts may be forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 as amended the Securities Act, and Section 21E of the Securities Exchange Act of 1934 as amended the Exchange Act. Forward-looking information is inherently subject to risks and uncertainties and actual results could differ materially from those currently anticipated due to a number of factors, which include but are not limited to the factors set forth in documents filed by us with the Securities and Exchange Commission from time to time, including without limitation on our annual report on Form 10-K and interim reports on Form 10-Q. Forward-looking statements may be identified by such terms as may, will, should, could, expects, plans, intends, anticipates, believes, estimates, predicts, forecasts, potential, or continue or similar terms or the negative of these terms. Although we believe that the expectations reflected in the forward-looking statements are reasonable, we cannot guarantee future results, levels of activity, performance or achievements. We have no obligation to update these forward-looking statements.

Roberta Lipson, Chief Executive Officer and President

Thanks, Larry. We announced our results for the third quarter and first nine months of fiscal 2010 in a press release this morning, which included our income statement, balance sheet and divisional results for the quarter and nine months period. We will use this call to summarize our operational results and to take some of your questions.

For the first nine months of fiscal 2010, revenue increased 16% to $129.9 million, operating income tripled to 13.3 million and our net income was 7.7 million or $0.48 per diluted share.

For the third quarter, revenue was up 12% on a year-over-year basis to 46.5 million. Our operating income was $6.6 million and our net income was approximately 3.9 million or $0.24 per diluted share. Our third quarter results reflect a substantial increase in profitability, which included a $3.3 million business tax refund, which was accounted for as a reduction in operating expenses for the quarter. Net of this tax refund, our net income for the quarter is still almost double that of the same quarter last year.

The Chinese government has revised its rule regarding exemption from business tax. Now, core profit Healthcare Services entities are exempt from previously assessed 5% business taxes. Accordingly, our Healthcare Services division was entitled to refund the business tax paid since January 1, 2009 with continued exemption in future periods. We are extremely pleased to see this refund and ongoing exemption. We believe it illustrates ongoing support for our efforts to provide premium quality care in the private sector alongside China's healthcare reform initiatives in the public sector.

Outside of this substantial benefit to the bottom line, our financial results were in line with our projections, but do illustrate some near-term challenges in both Healthcare Services and Medical Products division.

In Healthcare Services, revenue increased 5% to 21.6 million and our operating expenses decreased by 13%, including the tax refund I just explained. The anticipated deceleration from the second quarter's revenue growth of 10% reflects the build-out of our BJU facility. We are extremely excited about the completed facility coming online later this year, and we expect to complete the construction in the fall of 2010. We are doubling the number of patient beds and [indiscernible] state-of-the-art operating rooms and adding several new services including neurosurgery and cardiovascular care as well as expanding our orthopedic sports medicine and infertility department.

However, until the completion of the expansion project this fall, we'll continue to see the effects of this reduced capacity and much pressure on patient growth. We are on track for the formal opening of the New Hope facility this spring and we continue to ramp up our oncology efforts. We have already begun to witness increasing patient volumes in this area.

At our Guangzhou facilities, we continue to drive increasing patient revenue. The new joint-venture hospital is progressing well through the design and construction approval stage, and we believe there is the possibility of augmenting the space we have in the near future.

As our business in the Shanghai hospital continues to grow, we are assessing new facility sites in Pudong. Additionally, we are pleased to report that in Tangshan, a city located near Beijing, we have recently initiated a development project for our future hospital facility.

Overall, our vision remains the same. We are confident in our value proposition to provide premium quality healthcare in China and we're committed to rolling out our United Family business model in existing cities, as well as in second-tier cities over time.

In the Medical Products division, third quarter revenue increased 18% year-over-year to $24.9 million. We continued deliveries under our current KfW Development Bank contracts and this generated approximately $3.2 million in revenue during the third quarter.

So far this year, our KfW contract have generated 7.5 million in revenue, which is on track with our internal projections. Now that year-over-year revenue performance reflects more KfW activity in the year ago period, and keep in mind that our fourth quarter fiscal 2009 included exceptionally strong KfW activity as well. So we will have a tough comp in our March quarter.

Moving on to daVinci sales, we are pleased to report that we have recognized two daVinci sales for the third quarter. Both of these were placed into army hospitals, which are subject to an approval process somewhat removed from the Ministry of Health.

We have said consistently that quarter-to-quarter results for this division vary dramatically due to timing of shipments. This is certainly the same case as of today. The Ministry of Health normally reviews the import approvals for Class A medical capital equipment to public hospital customers. And as of today, we are awaiting approvals for additional daVinci sales. We expect to see additional approvals take place, but we cannot give timing at this point.

We do have confidence however that the current delay is not indicative of the market opportunity and we believe there is considerable long-term demand for our robotic surgical systems in China.

We experienced some challenges in sales of our other medical products during the fiscal third quarter. We believe these factors are temporary and that the general market conditions for healthcare devices in China is a compelling long-term opportunity.

Specifically, the introduction of a new generation of technology and diagnostic ultrasound was more than expected and this impacted sales of other products during the quarter. We also began to wind down our clinical chemistry distribution relationship with Johnson & Johnson during the quarter. They have been a partner for many years. However, following the expiration of our last distribution agreement, we were unable to come to an agreement on future growth investment objectives. We have been active in the clinical laboratory markets for many years and we are already working on registration for new product offerings in that category.

Our MPD portfolio is robust and we are currently in discussions with most of our medical technology leaders that would bring us exposure to new therapeutic areas in 2011. These include surgical navigation, imaging monitors, oncology and cancer detection.

Overall, our third quarter results reflect continued growth in our hospital division, offset by some capacity constraints and construction in Beijing and temporary challenges in our Medical Products division, most of which are related to Class A review.

I'll now turn the call back to Larry to review the financial results for the quarter.

Lawrence Pemble, Executive Vice President and Chief Financial Officer

Thanks, Roberta. Our 10-Q will be filed today and you can also find a detailed overview of our financials in our earnings press release. So I'm going to point out some key highlights.

In the Healthcare Services division, revenue was 21.6 million, an increase of 5% over the prior-year period, and the division reported income from operations of 5.6 million, up substantially from 2.2 million in the prior year. As Roberta mentioned, operating income in this division reflects a 3.3 million benefit.

For the Medical Products division, revenue increased 18% to 24.9 million from 21.1 million in the prior-year period. Revenue growth during the period reflected the increase in sales in women's health imaging products and the delivery of two daVincis.

Due to the general slowdown in growth rates for imported medical devices in China and the impact of the introduction of a new generation of technology in diagnostic ultrasound, which replaced the previous market-leading product, sales of some of our products during the quarter were lower than the prior year.

During this quarter, we recorded revenues of approximately 3.2 million under our current KfW Development Bank contacts.

Gross margin in the division was 29%, in line with historical averages. The division reported income from operations in the quarter of 1.3 million compared to a loss of 630,000 in the prior period.

Overall, our results reflected approximately 269,000 or $0.02 per diluted share of development and start-up expenses in our hospital division and non-cash stock compensation expense of 888,000 or $0.05 per diluted share. The tax refund accounts for approximately $0.15 per diluted share.

As of December 31, 2009, our unrestricted cash, cash equivalents and investments were 81.4 million, which included 23.8 million in cash and equivalents, and 57.7 million in current investments.

Our accounts receivable declined slightly to 40.3 million from 41.7 billion at the end of the prior period, but still significantly above historical averages due to both strong end of quarter sale, and along with the normal AR days related to the collection cycle of government loan contracts.

We also provided our nine-month financial results, hence we believe they highlight our progress in the first nine months versus this time last year. Specifically, revenue increased 16% to 129.9 million from 111.8 million. Operating income increased to 13.3 million from 4.3 million, and net income increased to 7.7 million from 1.5 million in the prior year period. This leaves me to our expectations for the remainder of the year.

We anticipate revenue growth of roughly 8 to 10% in Healthcare Services and we anticipate year-over-year revenue performance that is roughly flat in the Medical Products division. This is down from our prior expectations of low to mid-teens growth in both divisions.

Several factors we have mentioned to driving our updated expectations today. Specifically in Healthcare Services, 8 to 10% year-over-year growth reflects continued volume increases across our network was offset by the build out of our BJU facility. While the construction will greatly expand capacity for the long run, it just continued to dampen our annual performance for the year.

In the Medical Products division, our expectations were roughly flat. Revenue performance reflect first, the overall market slowdown in 2009 for imported medical products, which was the lowest growth rate we can recall, totaling only 8% for the year versus growth consistently in the mid-teens and higher.

Second, our belief that we will not recognize any additional daVinci sales in the remainder of the fiscal year, we do see continued demand and we believe that market for daVinci is increasingly robust, so we believe the long-term sales opportunity is compelling, but the budgeting and approval cycle of the Ministry of Health Class A review should impact our near-term sales performance. This accounts for the majority of our adjustment to guidance in this division.

Third, as we mentioned, we are also experiencing a slower than anticipated ramp-up with new ultrasound equipment. This is due to product life cycle and new product technology introductions, which are to be expected. The cycle of this process has been extended somewhat by the market factors of healthcare reform and macroeconomic trends over the past year.

Lastly, as we mentioned, we are facing out of the clinical chemistry product line with J&J. The wind down of the J&J chemistry product line will be substantially complete by fiscal year end. Our current year operations will reflect to reduction in revenues relative to expectations over the second half of the year, which will be offset by the sale of equipment inventories.

That concludes my comments on the finance side. We will now -- I'll turn the call back over to Roberta.

Roberta Lipson, Chief Executive Officer and President

Thanks, Larry. Before we go to Q&A, I'd like to reiterate the opportunity for Chindex created by healthcare reform in China. Healthcare reform continues to be an important issue here in China.

We believe that the government and media focus on healthcare reform increases consumer awareness about the quality of healthcare available both from the public and private sector with the growing emphasis on premium services being provided by the private sector.

We also see signs from the government of increasing willingness to support our Healthcare Services investments with attractive preferential policies such as the business tax exemption we were awarded.

That concludes the pre-recorded portion of our call and we'll now open the floor for live Q&A.

QUESTION AND ANSWER SECTION

Operator: [Operator Instructions]. We'll take our first question from Hamed Khorsand with BWS Financial.

<Q – Hamed Khorsand>: Good morning. Just trying to get an understanding here, you're right now talking about daVinci not being placed in the March quarter and we're right now beginning at February. What's taking so long as far as delay process? I'm wondering just being more streamlined as we've been importing daVinci over the past few years now?

<A – Roberta Lipson>: Hamed, this -- thank you for the question. It totally has nothing to do with demand. Demand is strong and growing and there is a big pipeline. It has to do with the government approval process and the Chinese government has a regulation that any civilian hospital that wants to buy a certain set of products, for example, daVinci surgical robot, Cyber Knife, Gamma Knife, all have to be approved by the Ministry. And the Ministry convenes a meeting twice a year and approves hospitals.

And because we're in the middle of this big healthcare reform thing that says we have to find a way to lower the cost of healthcare, they don't want to be seen now as approving a whole bunch of very expensive equipment. And so whereas in another time, they may have made exceptions and made approvals in between meetings. And sometime in the future I think that -- I think that there might be a time when they are willing to make exceptions or maybe approve a quota for the year, and as long as you are under the quota, it's okay to keep importing them. But right now it's a very sensitive time for healthcare reform and I think that unfortunately that's the whole topic. We don't expect the Ministry to have another meeting until this spring, and as far as we know that's the April-May timeframe, it could possibly happen before that. And just as we've seen some military sales takes place without -- in another context in that meeting approval, that could also be happen in the future. So this is totally out of our hands, and as I said, has nothing to do with the pipeline of demand, which is extremely strong and become stronger as time goes on.

We have a lot of doctors doing papers, holding meetings, going to international conferences and talking about their experience in China, every other hospital that has a major surgery department is totally jealous if they don't have a daVinci yet. So it's an exciting pipeline of demand, but right now it's -- the valve is at the ministry and then only can [indiscernible] twice a year for civilian hospitals.

<Q – Hamed Khorsand>: Okay. Understood. And just a follow-up on that is, would that suggest that you can have just cycle back, the June quarter, you could essentially place six units and not place anything in the next quarter proceeding that. Is that kind of --

<A – Roberta Lipson>: Well, as I said, I am hoping that next year as the focus goes to the next phase of healthcare reform that we might see some more flexibility and a capability of having smoother quarters. But I won't take that out of the room of possibility. Yes, it could be the way it plays out.

<Q – Hamed Khorsand>: Okay. And then also, what does Johnson & Johnson represent as far your Medical Products revenue?

<A – Roberta Lipson>: It was not a significant number. Yeah, so that's -- we don't report it separately. It wasn't a significant number and it was a situation that it was becoming much less interesting from a cash flow perspective, demanding a lot of use of cash with hospitals paying for the consumables in a very slow way. So the kind of investment that it demanded made it a less and less interesting business for us.

<Q – **Hamed Khorsand>:** Okay. And then my last question is, what's the current cash needs for your Healthcare Services buildout, and what have you spent and what do you need to spend to finish it up?

<**A – Lawrence Pemble>:** Larry, you want to take that one?

<**A – Lawrence Pemble>:** Yeah, Hamed, hi, it's Larry. I think our current -- our forward 12 months CapEx is about 38 million and the majority of that obviously is development expenditures in Beijing. So that's the general and that -- so I think, does that answer your question? I think it's about 38 million over the next 12 months.

<**Q – Hamed Khorsand>:** Yeah, that works. Thank you.

Operator: We'll take our next question from Mark Zinski for 21st Century Equities.

<**Q – Mark Zinski>:** Yes, good evening.

<**A – Lawrence Pemble>:** Hi, Mark.

<**Q – Mark Zinski>:** I just had a question about the medical equipment business. Can you comment on whether you've seen more increased activity in some of the multinationals in terms of having an interest in using your distribution services?

<**A – Roberta Lipson>:** This is kind of thing that ebbs and flows. Actually, I think it's worth noting that medical equipment imports in China, the growth in imports were the slowest we've seen them in many, many years of -- if you look at the whole 2009 over 2008. That having being said, I think China is the strongest market for all of the multinational medical equipment manufacturers now are looking to China as the great hope for the near future. And so there's certainly increased competitive pressures here among all of the players, whether they are looking for more interest in distribution, we see as I say, it ebbs and flows between interest in this kind of fragmented approach to distribution to more interest in working with the strong national player like us. And it seems to -- the fashion seems to come in and out depending on various market factors and political factors. And I can't say that I see it's going very strongly in one direction or another right now.

<**Q – Mark Zinski>:** Okay. And then sort of in that same vein [ph] in regards to the mammography, I guess controversy you'd call it, is China tending to pretty much mere [ph], in your opinion, western healthcare patterns, or are they just sort of developing kind of a more autonomous, I guess the opinion on the medical validity of, for instance, mammography?

<**A – Roberta Lipson>:** Well, that's a really interesting question. Actually China is so far behind the U.S. in earlier [ph] screening. That it's not a matter of whether it's 35, 40 or 50-year, all this appropriates to just start screening. It's just a matter that while may and we haven't done much screening, and breast cancer rates are going through the roof. But more importantly, the mortality rates are going through the roof. So there is a real recognition here that they've missed the both by not doing the early detections. And so there was such sort of low population of mammography per capita that -- mammography machines per capita that we've seen a real surge and interest, and some really strong growth on the mammography front.

<**Q – Mark Zinski>:** Okay. And Larry, can you comment on what the capacity level is for the hospital division, given the various expansion projects, is that what you say 75%, something in that neighborhood?

<**A – Lawrence Pemble>:** I am not sure I understand what you mean capacity. Something like utilization or something like this?

<**Q – Mark Zinski**>**:** Yeah, capacity utilization.

<**A – Lawrence Pemble**>**:** Yeah. Well, I think in general we are running capacity probably in the 50 to 60% range overall network-wide. And that's a little bit higher in Beijing and a little bit lower in Shanghai due to the nature of the evolution of those facilities. So I think that's -- and that's -- in Beijing in particular, we're getting up toward the capacity levels where we are anxious to have our new 70-beds open because we're at a -- when a healthcare facility gets 80% utilization, that gets close to what's called red-bed status where you don't have enough beds for your patients theoretically and so you need to have more. So we're right at the top level in Beijing, the comfortable level and that's why we're racing forward with the development plans there. Shanghai is a little bit ways to go from that -- from the utilization perspective. And I think that's probably where we are today.

<**Q – Mark Zinski**>**:** Okay. And do you have a start-up cost estimate for the current fiscal year on an EPS basis? I think indicated about $0.02 in start-up costs for the quarter. [indiscernible] what it was?

<**A – Lawrence Pemble**>**:** [indiscernible] on a nine months basis so that I can get you this number really quickly. I think it's a little over 900,000, EPS, I can do the math. I don't have it right at the tip of my tongue, but it's -- I can get you the year-to-date number very quickly.

<**Q – Mark Zinski**>**:** No, that's fine. And just last question. Any update on the SFDA approval for Biotest AG?

<**A – Lawrence Pemble**>**:** Still working through that process. When they have chemistry product like that, they actually have to go through clinical trials. So I think we're probably in the nine to 12 months range still at this point in time.

<**Q – Mark Zinski**>**:** Okay. Great. That's it from me. Thank you.

Operator: [Operator Instructions]. We'll go next to Gregg Hillman with First Wilshire Securities Management.

<**Q – Gregg Hillman**>**:** Yeah. Good morning, Roberta and Larry.

<**A – Roberta Lipson**>**:** Hi, Gregg.

<**A – Lawrence Pemble**>**:** Hey, Gregg.

<**Q – Gregg Hillman**>**:** Hi, I have a question, remember what one of your early comments saying the new -- that Beijing was adding 70 beds. Was that including the Beijing campus and New Hope?

<**A – Roberta Lipson**>**:** New Hope is actually an outpatient facility.

<**Q – Gregg Hillman**>**:** Okay.

<**A – Roberta Lipson**>**:** And so it really the extension of the Beijing campus. But I need to stress that we won't be opening all 70 beds at once [indiscernible] or adding.

<**Q – Gregg Hillman**>**:** Okay. And then just this new expansion in Guangzhou, Beijing, and I guess New Hope. Is that going to increase your earnings capacity, the company -- while, for the hospital services division by 50% or more would you say?

<A – Roberta Lipson>: Well, Guangzhou is not opening until 2012. That's a Greenfield facility. That's still in the early for this design phase. But yeah, I mean I think that over time, certainly the capacity is increasing by certainly something like that.

<Q – Gregg Hillman>: Okay. And just a question about your revenue. Have you ever broken down revenue for the hospital services between clinics and hospitals, or do you care to do so?

<A – Roberta Lipson>: Well, of course we do so internally, but we don't publicly report that. I think it's important to note that stand-alone outpatient clinics are not a huge revenue producer and then of themselves, and their importance really is just intake points and referral points for the hospitals. And so it really so there is a wider geographic net of convenience for our patients to use our services and if they need to be hospitalized, it will come to us. And in the U.S., hospitals develop relationships with private practice doctors for that purpose, but in China there are no private practice doctors. So we have to be our own referrals services.

<Q – Gregg Hillman>: Okay. And just a question about the built out for some of the new hospitals in terms of -- could you just talk about the timetable either in Guangzhou or some of the other or Tangjie [ph], what would be the, I don't know, the build time, the time to breakeven and the time to, I don't know, 50% utilization. Could you --?

<A – Roberta Lipson>: Well, it all -- it varies very much by project-by-project whereas Guangzhou is complete Greenfield facility, and from now we're at early design stage. It will be at least three years before that hospital sees the light of day, probably two-and-a-half -- well, the light of the day, it will see, but patients, it will be a little bit over two years. Tangjie is calendar year 2011, there is a show of a building, but there still are approval processes and build out processes that need to happen. New Hope is opening this spring. The Beijing expansion will be finished in the fall. And so it depends on what -- if it's acquisition of an existing building that needs to be renovated or it's a from-scratch buildout or it's just a clinic, which could take just a few months, if it's an office-based clinic as opposed to a greenfield hospital, which could take three years. So it really differs facility-by-facility and probably the break-even point also differs -- varies by the geographic region, the level of demand et cetera. Many of our facilities have become casual, neutral in the second year and profitable after the second year. Yeah, so that's -- I hope that's the guideline for you. I am afraid due to travel; I am going to have to jump off of the call. So Larry is going to continue to answer questions for you, and then if there are more questions, specifically for me, I'm available through Ashley or directly after the call today.

<Q – Gregg Hillman>: Great.

<A – Roberta Lipson>: Okay.

<Q – Gregg Hillman>: Thanks, Roberta.

<A – Roberta Lipson>: All right. Bye, bye now. Yeah.

<Q – Gregg Hillman>: Larry?

<A – Lawrence Pemble>: Gregg, do you have anything else?

<Q – Gregg Hillman>: Yeah, just one more question if I could, Ashley, please. Just for Guangzhou, I mean, in a way it's a test market for you in addressing -- solely Chinese population and would you consider that or I mean, I guess you have a successful clinic. Do you have any reason to believe that it would be successful or do you think it's an important market test going after new population for your company?

<A – Lawrence Pemble>: Well, certainly I think from the beginning of United Family Healthcare, we've been doing a lot of study of the Chinese market demographics that we are targeting. So the -- and Guangzhou is the third major city that we are entering. We've been doing, had significant increases in Chinese patient centricity in our existing markets, in Beijing and Shanghai over the years, and are now moving into a more aggressive development plan specifically in -- for the Chinese market and the buildout in Beijing, as we've talked about, puts services in our network that are specifically Chinese market-oriented such as neurosurgery, cardiothoracic surgery, outpatient oncology treatment and things like this are much more Chinese market-oriented than primary care, which has been our service model for many years in both facilities. So the market potential for the network buildout is certainly in the Chinese market there. It is different than the expatriate market, the needs of the patients are different, the clinical standard that we're looking to project remains the same, we are a JCI-accredited network and believes that the quality of the service will define the ultimate market demand in a very substantial way and the market work that we've done relative to the demographics and segmentation of the market is clearly there, that the market for this level of service is there in every major Tier 1 and Tier 2 city in China. So I think that the -- from our perspective, the rollout is moving along just the way we've kind of anticipated it would.

<Q – Gregg Hillman>: And finally, Larry, I think you mentioned you're -- I believe you're going to charge a lower price for the services to the Chinese population in some of the cities? Is that correct, and would that result in less margin on a unit basis on a patient basis?

<A – Lawrence Pemble>: No because interestingly enough our price sensitivity testing has shown that greater market access is there at a slightly lower price point. Our flagship facilities in Beijing and Shanghai are bilingual environments, and the revenue -- the price point will come down, the cost will also come down. The cost of maintaining an English-language environment in Beijing and Shanghai is quite high. If we don't need to have so many bilingual nurses and physicians on staff, the cost of providing the service goes on. So we don't expect the margin to just stay into the impact actually. Higher revenues due to increased volumes, higher operating margin, higher operating profit due to similar economics in the model as the price and costs come down.

<Q – Gregg Hillman>: Okay. Thank you.

Operator: We'll take our next question from Hongbo Lu with Piper Jaffray.

<Q – Hongbo Lu>: Thank you. Hey, Larry. How are you?

<A – Lawrence Pemble>: Hi, Hongbo, how are you doing?

<Q – Hongbo Lu>: Good. Good. I have quite a few questions. I jumped off in the middle and maybe missed part of the prepared remark. Just first question is on the growth margins for the Healthcare Services. It improved significantly and then my expectation was gross margin for this part of business might under pressure due to ongoing expansion, so I just want to get your thought on that one?

<A – Lawrence Pemble>: Yeah. Where we did I think that we've -- if we look at it, we don't publish the discrete market growth rates but the adjustment, the guidance that we announced today is largely driven as we've disclosed for the last couple of quarters in Beijing. I think we're very anxious to get these new services on line. The growth rates have been attenuating in Beijing over the last several quarters. Shanghai on the other hand, has been continuing in excess of expectations, I can say it that way. So it has everything to do with the relative size of Beijing to the divisional results being the lion share of divisional results and the attenuating growth curve as we bring these new facilities on line.

<Q – Hongbo Lu>: So I was asking about gross margin.

<A – Lawrence Pemble>: Oh, the gross margin? Excuse me --

<Q – Hongbo Lu>: Yes.

<A – Lawrence Pemble>: The -- let me -- I think we're doing quite well, right. I think we're --

<Q – Hongbo Lu>: Yeah, yeah, exactly. And now I just want -- I think in internal gross margin for the health services this quarter is quite significant?

<A – Lawrence Pemble>: Right. Well, we do have -- you need to net it -- net the form of -- to get an apples-to-apples comparison you need to net the 3.3 million benefit. I mean, we did have this tax rebate, the business tax rebate, not in income tax, business tax. It's a credit to operating costs in the period. It is applicable to the entire calendar year but it was not evident that this would actually happen until this quarter. So we took ...

<Q – Hongbo Lu>: Okay.

<A – Lawrence Pemble>: ... a year-to-date -- the cumulative benefit in the third quarter. Going forward, we do have an improvement on the operating margin. Being exempt from the business tax, we'll realize relative to historical performance, we will see an improvement of approximately 5% on the operating expense line. That was the value of that business tax. It was 5% of revenue.

<Q – Hongbo Lu>: But that that tax is actually coming out of operating expenses, right. That benefit -- but the gross margin for the healthcare services this quarter was improved? Did I get my number wrong?

<A – Lawrence Pemble>: What is the number you're showing then?

<Q – Hongbo Lu>: The gross margin I'm showing is 31%.

<A – Lawrence Pemble>: Gross, G-R-O-S-S, right?

<Q – Hongbo Lu>: Yes.

<A – Lawrence Pemble>: Yeah. Well, right, we have revenue of 21.5 and income from operations of 5.6, correct?

<Q – Hongbo Lu>: Well, yeah. Well, let me see. So the revenue is 21.5 and then COGS, cost of sales for the healthcare services is about 14.7, right?

<A – Lawrence Pemble>: Right. But to get it, what I'm saying, Hongbo, maybe we can follow-up on the details ...

<Q – Hongbo Lu>: Yeah.

<A – Lawrence Pemble>: ... after the call. But to get a -- what you need to do really to get a clear picture, yes, that 14.7 is inclusive of $3.3 million benefit. So ...

<Q – Hongbo Lu>: Oh! I see.

<A – Lawrence Pemble>: ... on an apples-to-apples, you need to back that out or back all about 5% of it out, and then you're looking at ...

<Q – Hongbo Lu>: Yeah, yeah, yeah. I think I know what you're meaning now, Larry, sorry about that. Okay. Secondly that -- about the decelerating imported medical product sales in China that you mentioned, where was this sourced of that? I think you are making the statement on the broad market from a broad market perspective, right, not just [indiscernible]...

<A – Lawrence Pemble>: That's over -- yeah, right. That's overall custom statistics year-on-year. Chinese custom statistics for the imported medical devices market ...

<Q – Hongbo Lu>: I see, I see.

<A – Lawrence Pemble>: So where -- yeah.

<Q – Hongbo Lu>: Okay. And then do you think it has anything to do with more and more multinationals actually are manufacturing their own products in China, because both Philips and GE, they've reported very quite strong sales in China through the quarters ...

<A – Lawrence Pemble>: Sure.

<Q – Hongbo Lu>: ... this year?

<A – Lawrence Pemble>: I think what we've seen we actually did a fair amount of research about this just a couple of months ago. We're seeing, yes, you're right, on the multinational basis, the percentage of domestically supply product is increasing relative to the imported devices over time. Both market segments are still growing quite robustly if you look at historical trends. But the percentage of the market that supply domestically versus from imports is increasing, and multinationals are, you're absolutely right, they're not -- they are participating more and more in the domestic side of things through local supply. Our -- the part of the market, the segment of the market that we participated in the imported devices has continued to grow at a fairly robust clip as we've mentioned in the release. Normally we would see a mid to high-teens or even -- and even higher this year for variety of factors. We're down to about 8%, but we don't -- that's not because of the import market is deteriorating for relative to the domestic market, and we believe those are temporary factors due to healthcare reform and things like that.

<Q – Hongbo Lu>: Okay, okay. And then two questions more on the macro side, but we can always go back to Roberta if we need to. Why is for the bank -- the China, the bank lending tightening practice in policy or measures that's happening in China, do -- should we expect any impact on top-tier hospitals ability to excess capital and buy expensive equipments?

<A – Lawrence Pemble>: I don't think so. Actually it is true that bank lending has been halted. There was an announcement recently. But traditionally, Chinese hospitals have not bought capital equipment through debt secured locally in China. They'd -- it was only very recently through the economic stimulus package following the economic downturn that that the bags began aggressively looking for business and turning to Chinese hospitals to extend credit for the purchase of equipment. That's a very unusual thing historically. Historically Chinese hospitals have purchased capital equipment out of retained earnings, and have not been -- have not secured a lot of debt locally in China.

<Q – Hongbo Lu>: Okay.

<A – Lawrence Pemble>: So, answer to your question, I don't think -- yeah, I don't think it will see -- I think it will have any impact in the medical devices business per se.

<Q – Hongbo Lu>: Okay. Sounds good. And also lastly, the recent public hospital reform guidance that was released from the Chinese government, have you seen any material -- anything substantial that we can expect a material acceleration in the privatization of Healthcare Services sector in China?

<A – Lawrence Pemble>: I don't think so. The pilot program is out there for public hospital reform, and kind of the keystone of that being kind of winning the hospitals off of pharmaceuticals, saving of the profits from the sale of pharmaceuticals is really kind of the cornerstone of that process. It's been -- we've been trying to do that for many, many years now already. Hopefully this reform process will have more success than the prior ones you have had. But I don't think it's far enough along to be able to project kind of an accelerated rate of privatization or anything that would start to really impact the market as in the aggregate at this point, still pretty early in the process, I think.

<Q – Hongbo Lu>: Okay. Great. Thank you so much, Larry.

<A – Lawrence Pemble>: Okay. Thanks, Hongbo.

Operator: We'll next to Andy Wu with JMP Securities.

<Q>: Hi, Larry. This is Andy.

<A – Lawrence Pemble>: Andy, how are you?

<Q>: Good. So just a quick question on the business tax exemption. So how long would the exemption last going forward?

<A – Lawrence Pemble>: We hope forever, we expect forever. It's actually been the underlying policy of the government for a long time that was superseded by some central government determinations that -- so actually in a way if you kind of track the kind of the legal aspects of it, they've kind of gone back to a policy that was -- has been in existence for a long time. So we do not expect this to be turned back again for a long time. The compromised solution was a three-year exemption upon the formation of a new for-profit Healthcare Service entity and now they've gone back to no limitation on that exemption at all.

<Q>: Okay. That's good. So I assume that that's applied to the entire Healthcare Service division, not just the BJU facility.

<A – Lawrence Pemble>: Correct.

<Q>: So for the upcoming [indiscernible] facility, the New Hope, this will apply [indiscernible].

<A – Lawrence Pemble>: Yes, everything. Correct.

<Q>: Second question on the Medical Products division. So one of the reasons you mentioned as far as this flat projection is the ramp-up of the new ultrasound treatment. So can you give us some color on how long do we expect this ramp-up period will be? How long this --

<A – Lawrence Pemble>: Well, I think we -- well, I think we are kind of gradually coming out of the cycle. I think when you have a -- I think you need to understand a little bit about the composition of a premium grade color Doppler ultrasound that the Siemens product that had been in existence for many, many years, was the market-leading product in the high-end of the market. And still even at the -- although the price point for that product had become like as natural end of technology life cycle on the -- and the price point has been coming down over the last several years. But the technology itself, the basic clinical utility of the technology was still at the top of the market.

And so the new -- this new technology platform comes in, re-establishes or tries to re-establish a significantly higher price point for an incremental, not the incremental, but a significant technology growth, a new technology platform. But the -- and at the same time, we have healthcare reform and the overall downturn in the Chinese economy that have been running through everyone's numbers for the last several periods. And as with any new product, new technology introduction, there are a cycle as a new technology is released, a sequential product revisions, the early -- the 2.0s go to 2.1 to 2.2s, and the sequence of those rolling out while the bugs [ph] are worked out and all the service offerings are integrated into the platform. All of that takes a little bit of time. So I think that what we've been experiencing is a pretty normal process and we are -- our results are improving the integration of the technology into the market is -- it's a quite a significant clinical jump from a technological and clinical standpoint. So we have great expectations as the Siemens for this technology platform, it's just taking a little while to get some traction at the high end of the market.

<Q>: Sure. That's helpful. Thanks.

<A – Lawrence Pemble>: Thank you.

Operator: We'll take our final question from Mark Zinski with 21st Century Equity.

<Q – Mark Zinski>: Well, I'm sorry, Larry. Just a quick clarification on the business tax, so that flows through the Healthcare Service cost line item?

<A – Lawrence Pemble>: Correct.

<Q – Mark Zinski>: Okay. And then obviously there wasn't a pass through tax spend?

<A – Lawrence Pemble>: Pass through tax, what do you mean?

<Q – Mark Zinski>: Just that mean it wasn't billable to the ...

<A – Lawrence Pemble>: No, no, no, no.

<Q – Mark Zinski>: No. Okay.

<A – Lawrence Pemble>: [indiscernible].

<Q – Mark Zinski>: Okay. Thanks a lot.

Operator: This will conclude today's conference, and we thank you for your participation.

Lawrence Pemble, Executive Vice President and Chief Financial Officer

Thank you, everybody.