

Management Discussion and Analysis

FINANCIAL REVIEW

During the year ended 31 December 2001, the Group's turnover grew by 25.26% and recorded approximately HK\$257,426,000, of which 60.31% and 39.69% were derived from the PRC and Taiwan segments respectively. Net profit of the Group for the year was approximately HK\$71,043,000, being an increase of HK\$910,000 over that of 2000.

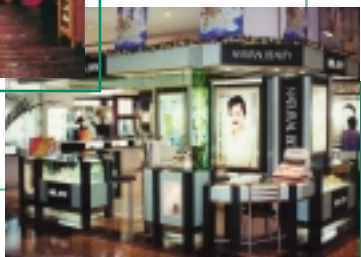
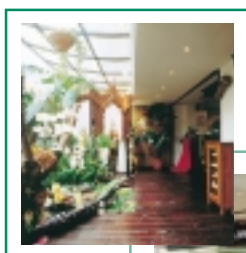
In the PRC, market demand for skin care, beauty and aromatherapeutic products and skin treatments and SPA services are expected to grow at an increasing rate when the average family disposable income continues to rise. To capitalize on this opportunity and for its long-term business development, the Group carried out a restructuring of its distribution channels by establishing and acquiring 25 subsidiaries in major areas of the PRC from December 2000 to July 2001. Prior to the restructuring, all products of the Group were distributed via a number of independent third party regional distributors to its franchisees in the PRC other than Shanghai region. After the restructuring, major distributors, operators or franchisees became the minority shareholders of the Group's newly established and acquired subsidiaries. Leverage on the local knowledge and connection of the minority shareholders, the restructuring is able to strengthening the distribution network and accelerating the regional development of the Group in the PRC. Those subsidiaries also serve as regional vehicles of the Group to manage its self-owned and franchised beauty centres. The Group's distribution channel restructuring has been proven contributable to its turnover that reached approximately HK\$155,256,000 in the PRC for the year ended 31 December 2001, representing a 73.38% growth over 2000. Despite there was a short-term suffer on the Group's operating margin ratio for the PRC segment as recognized by the management when the restructuring process took place, the Group still achieved net profit of approximately HK\$41,761,000 in the PRC for the year ended 31 December 2001, being 8.26% higher than that of 2000.

In Taiwan, turnover and net profit of the Group for the year ended 31 December 2001 were approximately HK\$102,170,000 and HK\$29,282,000, declining by 11.90% and 7.21% respectively, mainly due to the persistent economic downturn and devaluation of New Taiwan dollars. In terms of New Taiwan dollars, profits after tax from the Group's operation in Taiwan still grew slightly by 0.28%. The net profit margin ratio for Taiwan segment also improved from 27.21% to 28.66% when the management continued to exercise tight cost controls during the year.

Sale of skin care products totalling HK\$200,090,000 continued to be the major source of income of the Group and represented 77.73% of total turnover for the year ended 31 December 2001 and a 24.86% increase over that of 2000. Meanwhile skin treatments, beauty and SPA service income and sale of aromatherapeutic products increased sharply by 168.81% and 99.76% and arrived at HK\$20,741,000 and HK\$15,621,000, equivalent to 8.06% and 6.07% of total turnover respectively after the Group introduced its aromatherapeutic products and opened its first Natural Beauty SPA in 2000.

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As at 31 December 2001, the Group had net current assets of approximately HK\$100,801,000. Current assets comprised cash and cash equivalents of approximately HK\$76,110,000, short-term investments of approximately HK\$65,750,000, inventories of approximately HK\$52,674,000, trade receivable of approximately HK\$27,416,000 and receivables, prepayments and other current assets of approximately HK\$36,952,000. Current liabilities comprised bank loans of approximately HK\$2,112,000, payables, advances from customers and other current liabilities of approximately HK\$130,779,000 and taxes payable of approximately HK\$25,210,000.



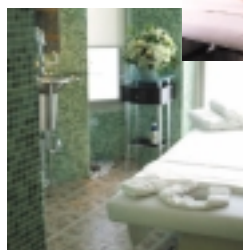
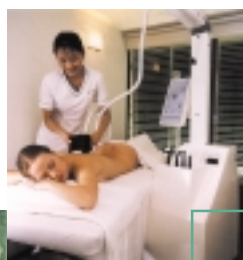
SALES AND DISTRIBUTION CHANNELS

The Group has three types of beauty centres, namely Natural Beauty SPA, NB Salon SPA and NB Beauty Salon, each offering a specific range of products and services, operating with unique decoration, operational area and facilities and targeting at different customer group. Since its establishment, the Group has formulated and implemented a large-scale franchise programme pursuant to which over 1,000 and 680 franchised beauty centres have been successfully established in the PRC and Taiwan respectively. Currently, each of the franchised beauty centres of the Group is either NB Salon SPA or NB Beauty Salon and all its 40, 12 and 1 Natural Beauty SPAs in the PRC, Taiwan and Hong Kong respectively are operated by the Group itself. The Group also operates 11 NB Salon SPAs and over 130 dedicated counters to sell its products and/or render its services.



PRODUCTS AND SERVICES

Through an extensive network of over 1,900 sales points in Greater China, the Group offers over 700 products under the brandname of "NB(r)", principally made of natural plant-extracted ingredients



imported from a number of countries including the United States and European countries like France, Italy and Germany. In general, the Group's products can be broadly categorized into four types namely (i) skin care; (ii) beauty; (iii) aromatherapeutic and (iv) others such as hair care, toiletries, fragrance, nutrition and brassiere products. The Group also provides an array of skin treatments and SPA services by applying exclusively its self-manufactured products and using specific equipment through a self-operated beauty centre network covering major areas of Greater China consisting of 53 Natural Beauty SPAs and 11 NB Salon SPAs manned by a number of professional beauticians being trained by the Group.



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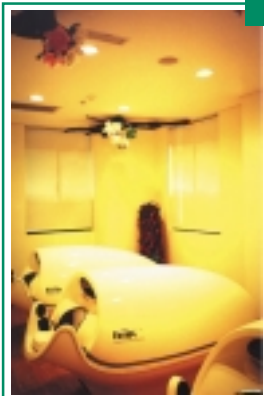
PRODUCTION FACILITIES

The Group owns two production plants, one located in Shanghai, the PRC with an aggregate gross floor area of approximately 3,465 sq.m. to manufacture products for international market save for the PRC segment and the other is located in Taipei, Taiwan with an aggregate gross floor area of approximately 3,209 sq.m. to manufacture products for the PRC market. Both production plants of the Group in the PRC and Taiwan have been accredited with ISO9002 and their current operating capacity has reached around 68% and 65% respectively.



QUALITY CONTROL

Pursuing the principle of “Good System, Good Technology, Good Products, Good Training and Good Services”, the Group emphasizes on hygiene and quality control over its raw materials, production process and finished products. The Group has formed quality control teams to examine the purchased raw materials on a random basis. Inspection is conducted on or after each critical production process to ensure that defective items are detected and remedied at the earliest possible opportunity. All finished products are also inspected before packaging with an aim to eliminating all sub-standard products. Quality data are recorded and quality analyses are carried out by the quality control team of each production line regularly, enabling the Group to take prompt action if any manufacturing problem occurs in the production process, thereby minimizing disruption to the entire process.



SALES AND MARKETING

High product penetration rate and wide geographical coverage are the keys to increasing product sales in consumer market. The Group has concentrated on selling its products through the beauty centres, enabling the Group to obtain a wide geographical coverage and promote its products to a large population of customers. The Group has also been able to reach retail customers directly through its dedicated counters in large shopping arcades and department stores in the PRC. To facilitate product penetration, the Group segregates its target markets into three segments namely premier, middle and mass markets and develops corresponding product lines marketed using different pricing and marketing strategies.

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RESEARCH AND DEVELOPMENT

In order to maintain its competitive edge, the Group takes research and development seriously with a view to improving the quality of its existing products and developing new products. The Group's research and development team comprising 13 members with experience and expertise particularly in cosmetics, pharmacy and bio-chemistry takes into account the feedback from customers and keeps abreast of new technology. Since its establishment, the Group has developed over 700 skin care, beauty and aromatherapeutic products and has, in 2001, launched 28 new products.

LIQUIDITY AND FINANCIAL RESOURCES

The Group generally finances its operations with internally generated cash flow. During the year ended 31 December 2001, the cash generating ability of the Group remained strong, with approximately HK\$134,808,000 being generated from operating activities. As at 31 December 2001, the Group had cash and cash equivalents of HK\$76,110,000 and short-term New Taiwan dollars bank borrowings of HK\$2,112,000 bearing interest at rates ranging from 7.35% to 7.70% per annum, which HK\$333,000 was guaranteed by a director of the Company. Subsequent to 31 December 2001, all short-term bank borrowings of the Group has been fully repaid and the relevant director's guarantee has been released.

The Group currently earns revenue and incurs costs and expenses mainly in Renminbi, New Taiwan dollars, Hong Kong dollars and United States dollars. The Company's financial statements are stated in Hong Kong dollars and the payment of dividends, if any, are also denominated in Hong Kong dollars. Accordingly, any significant volatility and depreciation of Renminbi and New Taiwan dollars could adversely affect the Group's business, financial condition and results of operations. The Group will conduct periodic review of its exposure to foreign exchange risk and use derivative financial instruments to hedge against such risk, as considered appropriate in the circumstances. During the year ended 31 December 2001, the Group had not used any financial instruments for hedging purposes.

As at 31 December 2001, the gearing ratio and current ratio of the Group as at 31 December 2001 calculated as a ratio of total borrowings to total assets and a ratio of current assets to current liabilities are approximately 1% and 164% respectively.

As at 31 December 2001, the Group had outstanding contracted capital commitments of approximately HK\$876,000 in respect of acquisition of property, plant and equipment.

As at 31 December 2001, the Group had no material contingent liabilities.

With the above resources and the proceeds from the Company's issue of new shares at the time of its listing on the Stock Exchange on 28 March 2002, which, after deduction of related issuance expenses, amounted to approximately HK\$254 million, the Group has adequate capital resources to finance its present business expansion program.

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EMPLOYMENT, TRAINING AND DEVELOPMENT

As at 31 December 2001, the Group has a total of 625 employees of which 447 are based in the PRC, 171 in Taiwan and 7 in Hong Kong. The Group always maintains good working relations with its employees and has committed itself to employee training and development. To promote and maintain the quality and consistency of the services provided in its self-owned and franchised beauty centres, the Group offers continuing professional training courses to the beauticians employed by the Group and its franchisees.

Remuneration packages of the Group are maintained at a competitive level and reviewed on a periodical basis. Bonus and share options are awarded to employees according to the assessment of individual performance and industrial practice.

In addition, the Group has adopted a share options scheme on 11 March 2002, for the purpose of providing incentives and rewards to eligible participants who contribute to the success of the Group's operations. The directors may, at their discretion, invite any employee or directors of the Group and any qualified persons as set out on the scheme, to subscribe for shares of the Company. Up to the date of this report, no share option had been granted under the share option scheme.

The Group's subsidiaries in the PRC have participated in defined contribution retirement schemes organised by the relevant local government authorities in the PRC and are required to make monthly contributions at 9% to 27% of the relevant PRC employees' salaries to the schemes. The Group's subsidiaries in Taiwan have pension plans for its regular employees, and are required to make monthly contributions at 2% of salaries into an account maintained with the Central Trust of China in the name of a pension fund monitoring committee as required by the relevant Taiwan laws and regulations. The Group has also adopted a provident fund scheme for its employees in Hong Kong as required under the Mandatory Provident Fund Scheme Ordinance.

