

## MANAGEMENT DISCUSSION AND ANALYSIS

### BUSINESS REVIEW

During the year, the operations of the Group has been adversely affected by the SARS. Nevertheless, after a series of remedial actions, the Group maintained a marginal increase in the turnover to approximately HK\$103.5 million as compared to approximately HK\$96.0 million recorded in last year. Net profit from ordinary activities attributable to shareholders for the year is approximately HK\$5.6 million (2002: HK\$27.5 million).

#### Textile products containing the BIOenergy® compound

Textile products containing the BIOenergy® compound remain the core product line of the Group and recorded a turnover of approximately HK\$69.0 million (2002: HK\$87.1 million). The sales of the Group's major product, Healthy Sleeping System, accounted for approximately 84.6% of total turnover of this product category. During the year, the sales of this product category was adversely affected by the outbreak of the SARS in the major cities of the PRC, especially in Beijing, Shanghai and Guangzhou. In order to minimize the adverse impact of the SARS to the sales, the management has decided to provide more support to the franchisees. The Group's staff were sent to help the major franchisees to provide more customized services to customers, including on-site products demonstration and delivery. Moreover, the Group also sponsored the franchisees the additional printing matters for illustrating the Group's health philosophy: "Drink, Eat and Sleep", as an alternative to arrange exhibitions during the SARS period. After a series of such remedial actions, the decrease in the sales of this product category was narrowed to approximately 20.7% as compared with the previous financial year. Moreover, sales rebates have also been offered to the franchisees.

Currently, the SARS was over. Together with a series of media promotion activities, the management believes that the sales of this product category will be back to the right track.

#### Ionised Water Apparatus

After one year of marketing promotion, the newly introduced Ionised Water Apparatus becomes another major source of income of the Group. The sales of the product achieved approximately HK\$29.1 million, accounting for approximately 28.1% of total turnover of the Group. Currently, the bottled water is popular in the PRC. However, the bottled water comprises problems including secondary pollution — water polluted during the bottling process. As a substitute to the bottled water, the demand for the domestic purified tap water is on the increasing ride. The Group's Ionised Water Apparatus has the functions of filtering and ionising tap water which can increase the effectiveness of water to human body than normal tap water. After the SARS, people generally become more conscious on health which will accelerate the degree of acceptance for the product by the market.

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In some developed countries, including Japan, similar products have been popular for many years. The concept of domestic ionised water consumption is still in the infant period in the PRC. The management sees great market potential for the product and believes that the sales of the Ionised Water Apparatus might be higher if without the SARS impact.

### Polypeptide products

On 5 May 2003, China Healthcare Science and Technology Association arranged experts of the healthcare industry to recommend ten products for increasing immunity to the front line professionals during the anti-SARS period. The Group's albumin polypeptide capsule is one of the recommended items which evidenced the public recognition to the product in the industry. The management believes that the outbreak of the SARS has generally aroused people's concern on bacteria immunity of human body which will increase the market demand for such kind of product in the coming period.

### Sales and marketing

Keeping pace with the economic development in the PRC, the Group has continued to expand its franchise distribution network. Up to 30 June 2003, the Group has appointed 222 franchisees (2002: 179) operating 387 stores (2002: 340) in 240 cities (2002: 179) throughout the PRC.

### Research and development

During the year, The Sport Science Research Institute of The State General Administration of Sports of the PRC (國家體育總局體育科學研究所) has issued testing reports for the effects of the products containing the BIOenergy® compound in facilitating the recovery of sportsmen after sporting events. The reports show positive results for which the Group's textile products containing the BIOenergy® compound comprise the functions of increasing the efficiency of sportsmen during the sporting events and the quality of sleeping. The management is considering to take a further step towards the possible application of the Group's textile products containing the BIOenergy® compound in the sportswear products to cope with the 2008 Olympics Games to be held in Beijing.

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### FINANCIAL REVIEW

#### Turnover

Total turnover of the Group for the year was approximately HK\$103.5 million as compared to approximately HK\$96.0 million, representing an increase of approximately 7.8%. The increase in turnover was mainly due to the outstanding performance of the Ionised Water Apparatus which accounted for approximately 28.1% of the Group's turnover. The Group's traditional product, Healthy Sleeping System, was still the major product contributing to approximately 56.5% of total turnover. The sales of other BIOenergy® products accounted for approximately 10.2% of total turnover and the polypeptide products approximately 5.2%.

#### Gross profit

For the year, the overall gross profit margin reported approximately 60.5% as compared to approximately 68.0% recorded in last year. The decrease in gross profit margin was mainly due to the new product mix in which the gross margin of the Ionised Water Apparatus was lower than the traditional product, Healthy Sleeping System.

In terms of individual product line, the Healthy Sleeping System recorded a gross margin of approximately 70.0% as compared to approximately 72.0% recorded in last year. The decrease in gross margin was due to the offer of sales rebates to those franchisees whose sales had met pre-determined level. The gross margin of the Ionised Water Apparatus was approximately 47.9%, slightly decreased from approximately 48.5% last year. Other BIOenergy® products achieved approximately 45.9%, higher than approximately 37.1% recorded in last year. The gross margin of the polypeptide products was approximately 54.6% as compared to approximately 57.6% recorded in last year.

#### Net profit

For the year, net profit from ordinary activities attributable to shareholders amounted to approximately HK\$5.6 million as compared to approximately HK\$27.5 million recorded in last year. The decrease in net profit from ordinary activities attributable to shareholders was mainly due to the employment of additional resources to maintain the normal sales and market share of the Group during the anti-SARS period.

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Moreover, as part of the Group's pre-determined development plan, additional resources were also devoted for the enhancement of the Group's existing franchise distribution network in training the staff and franchisees and the establishment of Vitop Health Technology Halls in Shanghai, Chengdu, Suzhou, Beijing and Hangzhou. Expenses incurred for these activities are for future growth of the Group but have been reflected as expenses in the current year. As a result, the selling expenses for the year increased to approximately HK\$33.2 million from approximately HK\$20.8 million recorded in last year.

In addition, net profit from ordinary activities attributable to shareholders was arrived after the deduction of approximately HK\$4.1 million of professional expenses incurred for the introduction of the Company's shares on the Main Board of the Stock Exchange.

### LIQUIDITY AND FINANCIAL RESOURCES

As at 30 June 2003, the Group had a current ratio of approximately 4.2 as compared to that of 4.0 as at 30 June 2002.

As at 30 June 2003, the Group had no banking facilities and bank loan, and the shareholders' fund amounted to approximately HK\$76.9 million. The gearing ratio of the Group was 0% (2002: 2%).

As most of the Group's monetary assets are denominated in Renminbi and Hong Kong dollars, the exchange rate risk of the Group is considered insignificant.

As at 30 June 2003, the Group did not have any charges on its assets.

As at 30 June 2003, the Group had no contingent liabilities.

The Group has recently entered into an arrangement to acquire a land in Nanxiang area of Shanghai to develop our sales activities in the major cities of the PRC. The acquisition will be funded from the Group's internal resources.

The management considered that the Group's satisfactory financial position and operating results can provide sufficient financial resources for further expansion of the Group's business operations, as when required. Should investment opportunities arise requiring additional funding, the management believes that the Group is in a good position to obtain the required financing on favourable terms.

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### SIGNIFICANT INVESTMENT

During the year under review, there was no significant investment held by the Group.

### MATERIAL ACQUISITIONS AND DISPOSALS OF SUBSIDIARIES AND ASSOCIATED COMPANIES

During the year under review, there was no material acquisition or disposal of subsidiaries and associated companies.

### EMPLOYEES AND REMUNERATION POLICIES

As at 30 June 2003, the Group employed a total of 390 employees, of which 385 are based in the PRC and 5 are based in Hong Kong. The total salaries and other remuneration (excluding directors' emoluments) of approximately HK\$14.3 million were incurred for the year. Remuneration packages comprised salary, mandatory provident fund, bonus, medical coverage and share options.

### OUTLOOK AND FUTURE PROSPECTS

Statistics show that, in 2002, the national spending on healthcare products in the PRC amounted to US\$2.4 billion while the global spending on healthcare products was US\$200 billion. This proportion was far behind the proportion of the GDP figures.

The demography statistics also show that the proportion of aged people in the PRC is increasing. The aged group people will be more conscious on their health conditions. Moreover, many Chinese are accustomed to have medical supplements. With the development of advance technology, many people will consume the medical supplements shifting from a traditional way (for example making herbal tea at home) to a scientific way (for example consuming capsules).

Facilitated with these favorable conditions, the management will continue to devote resources to consolidate the existing franchise distribution network, to build up a sophisticated management system and to keep close strategic relationships with the well-known scientific and academic institutions and renowned scientists for developing new proprietary technology. In order to keep the Group in a key position in the PRC healthcare products industry, we will adopt the following strategies:

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### Enhancement of franchise distribution network

The management will continue to appoint new franchisees to capture the market share in some unexplored cities of the PRC. Moreover, based on the analysis from our customer database, we will provide more professional advice to help the franchisees to operate their business more effectively.

### Further exploration of the market potential of Ionised Water Apparatus

With the initial success of distributing the Ionised Water Apparatus, the management realises that there exists great market potential for this kind of product. Currently, the product is designed for domestic use. The management decides to set aside resources to study the application of the product for medical and catering purposes. With many competitive advantages the Group has, the management believes that the Ionised Water Apparatus will form another main stream of products for the Group.

### Expertise in the Healthy Sleeping System

After years of promotion, the Group's major product, Healthy Sleeping System, was well accepted by the market based on which the Group is recognised as one of the leading enterprises in the industry in the PRC. In order to keep the current status, the management will distribute the products more professionally and aims for different classes of customers, for example the executive group.

### Further study of albumin polypeptide

During the anti-SARS period, experts have announced on the media that the polypeptide can strengthen the human immunity system. This can let the customers have more knowledge about the function of these kinds of product. The management believes that it has positive impact on promoting the Group's polypeptide products. With the ownership of the technology of manufacturing albumin polypeptide, the Group has more aggressive marketing plans for the product in the coming period.