

## Discussion and Analysis

### Financial Review

#### REVENUE AND SALES PROCEEDS

During the year 2005, operating revenue of the Group grew to approximately RMB1,214.7 million, a growth of approximately 54.6% or RMB429.2 million from RMB785.5 million recorded in the year 2004. The impressive growth rate was contributed by the same store revenue growth of approximately 19.1%, revenue contribution from the new stores opened in the year 2005 and post acquisition revenue of approximately RMB184.8 million contributed by stores acquired in the year 2005 pursuant to the Group Reorganisation.

Direct sales increased by approximately RMB148.4 million or 50.7% from RMB292.8 million recorded in the year 2004 to RMB441.2 million recorded in the year 2005. This increase is generally in line with the increase in total operating revenue, however at a slower pace due to the strong increase in the other categories of operating revenue. Commission from concessionaire sales improved to RMB577.5 million, an improvement of approximately 61.5% or RMB219.9 million from RMB357.6 million recorded in the year 2004. The increase was a result of strong sales performance of concessionaire brands in our stores despite the marginal decline of rates from 22.0% recorded in the year 2004 to 21.6% recorded in the year

2005, which was due to the lower commission rates from the new stores opened and stores acquired during the financial year. Consultancy and management service fees remain close to the year 2004 at approximately RMB47.7 million. Rental income grew to RMB65.5 million, a growth of RMB13.1 million or 25.0% from RMB52.4 million recorded in the year 2004 due to the increased floor space leased out by the new stores opened and stores acquired in the financial year. Other operating revenue during the year improved to RMB82.8 million from RMB35.5 million recorded in the year 2004, a growth of approximately 133.2% or RMB47.3 million. This growth was mainly driven by the increase of promotional income and the credit card handling fees.

The Group generated total gross sales proceeds received or receivable worth approximately RMB3,308.0 million. (comprising of direct sales, sales proceeds from concessionaire sales, rental incomes, consultancy and management service fees and other operating revenue). Gross sales proceeds for the year represent a growth of 60.9% or RMB1,252.1 million from RMB2,055.9 million recorded in the year 2004.

On a Proforma basis, the revenue of the Group grew by RMB409.7 million or 33.4% from RMB1,227.8 million recorded in the year 2004 to RMB1,637.5 million recorded in the year 2005. The same store revenues growth was approximately 22.3% and new stores opened contributed the balance of the growth. Gross sales proceeds in the year 2005 grew by approximately 29.2% to RMB4,623.0 million from RMB3,578.5 million recorded in the year 2004. Commission rate of concessionaire sales improved from 19.6% recorded in the year 2004 to 20.7% recorded in the year 2005 due to the increase commission rate charged by the maturing stores.

#### PURCHASE OF GOODS AND CHANGE IN INVENTORIES

“Purchase of goods and change in inventories” refer to the costs of sales for the direct sales. In line with the increase in direct sales, the costs of sales increased to RMB363.5 million, an increase of RMB119.8 million or 49.2% from RMB243.7 million recorded in the year 2004. The gross profit margin of 17.6% improved marginally by 0.8% from 16.8% recorded in the year 2004. The improvement was due to the lower purchasing costs resulting from the increase of direct sales volume.

#### STAFF COSTS

Staff costs for the year increased by RMB50.5 million or 72.3% to RMB120.3 million from RMB69.8 million recorded in the year 2004. The increase was contributed by the inclusion of staff costs for (i) the new stores opened and stores acquired during the year, (ii) the increase in staff force for the store design and business development department in line with the business expansion plans and (iii) the additional provision for incentives in line with the increase of revenue and profitability for the year 2005.

#### DEPRECIATION AND AMORTISATION

Depreciation and amortisation increased by RMB12.0 million or 23.0% to RMB64.1 million from RMB52.1 million recorded in the year 2004. The increase was contributed by the inclusion of depreciation cost for the new stores opened and the stores acquired during the year.

#### RENTAL EXPENSES

Rental expenses increased by RMB50.7 million or 95.3% to RMB103.9 million from RMB53.2 million recorded in the year 2004. The increase was due to the inclusion of the rental cost for the new stores opened and the stores acquired during the year, in particular the rental expenses of the newly opened Zhengzhou, Haerbin and Sichuan stores in the year 2005.

#### OTHER OPERATING EXPENSES

Other operating expenses which consist mainly of utilities cost, marketing and promotional cost, property management cost, general administrative cost and others increased by RMB48.5 million or 41.3% to RMB165.8 million from RMB117.3 million recorded in the year 2004. The increase is generally in line with the improved revenue and the inclusion of other operating expenses from the new stores opened and the stores acquired during the year.

### PROFIT FROM OPERATIONS

Profit from operations increased to RMB397.2 million, an improvement of RMB147.7 million or 59.2% from RMB249.5 million recorded in the year 2004. This is generally in line with the revenue growth and improved operating efficiency of the stores. As a result, profit from operations as a percentage to revenue also improved marginally to 32.7% from 31.8% recorded in the year 2004. The stores acquired in the year 2005 pursuant to the Group Reorganisation contributed approximately RMB41.5 million or 10.4% to the total profit from operations of the Group.

On a Proforma basis, profit from operations increased to RMB473.7 million, an improvement of RMB190.2 million or 67.1% from RMB283.5 million recorded in the year 2004. Profit from operations as a percentage to revenue also improved to 28.9% from 23.1% recorded in the same period of last year in line with the improved operating efficiency of the maturing stores.

### FINANCE INCOME

Finance income, which comprises of interest income, foreign currency exchange losses and net of interest expenses increased to RMB8.4 million, an increase of RMB5.4

million or 180.0% from RMB3.0 million recorded in the year 2004 due to the increased interest incomes from the placement of deposit with licensed banks in Hong Kong and the PRC following the IPO.

### SHARE OF PROFIT FROM AN ASSOCIATE

Our share of profit from Shanghai Nine Sea Lion Properties Management Co. Ltd, an associate of the Company, the share of profit grew from RMB0.4 million in 2004 to RMB0.5 million in 2005, an increase of RMB0.1 million or 25.0%.

### INCOME TAX

The Group's income tax expenses increased by RMB40.8 million or 44.8% from RMB91.0 million recorded in the year 2004 to RMB131.8 million in the year 2005. The increase was due to the overall increase in the profit from operation before income tax. This increase of income tax expense was however partly offset by the lower effective tax rate of 32.5% in the year 2005, a decline of 3.5% from 36.0% recorded in the year 2004 as a result of the inclusion of higher portion of non tax-deductible expenses in the year 2004 and the inclusion of profit from the stores with preferential tax rate such as the Guizhou, Xi'an Chang'an and Xi'an Shidai acquired in the year 2005.

### NET PROFIT FOR THE YEAR

In line with the increase in revenue, the net profit for the year increased to RMB274.3 million, an improvement of RMB112.4 million or 69.4% from RMB161.9 million recorded in the year 2004. The net profit margin improved to 22.6% from 20.6% recorded in the year 2004 due to the lower effective tax rate and the improved operating efficiency that resulted in the higher revenue growth rate than the growth rate of operating expenses. The stores acquired in the year 2005 pursuant to the Group Reorganisation contributed approximately RMB32.5 million or 11.9% to the net profit of the Group.

### PROFIT ATTRIBUTABLE TO THE COMPANY

Profit attributable to the Company increased to RMB248.0 million, an increase of RMB95.2 million or 62.3% from RMB152.8 million recorded in the year 2004. This is in line with the increase in revenue and the profit from operations for the year. The stores acquired in the year 2005 pursuant to the Group Reorganisation contributed approximately RMB26.4 million or 10.7% to the total profit attributable to the Company.

On a Proforma basis, profit attributable to the Company rose from RMB150.6 million recorded in the year 2004 to RMB290.7 million in the year 2005, an increase of RMB140.1 million or 93.0%, in line with the increase in revenue and profit from operations.

#### PROFIT ATTRIBUTABLE TO MINORITY INTERESTS

Profit attributable to minority interests increased by RMB17.1 million or 185.9% to RMB26.3 million from RMB9.2 million recorded in the year 2004 due to the increase of net profit for the year and the inclusion of profit from stores with higher percentage of minority interests.

#### LIQUIDITY AND FINANCIAL RESOURCES

With the net proceeds of approximately RMB1,074.1 million raised from the issue of new shares, the cash balance at the beginning of the year of RMB408.5 million and the net cash generated from operating and investing and other financing activities during the year of RMB597.8 million, the Group's cash and bank balance as at 31 December 2005 rose to RMB2,080.4 million. The Group was in net cash position of RMB1,846.1 million even after netting off the bank loans of approximately RMB234.3 million. Total debt to equity ratio of the Group expressed as a percentage of bank and other borrowings over the total net asset of RMB1,873.3 million was 12.5% as at 31 December 2005.

#### WORKING CAPITAL AND NET ASSET

The Group's working capital as at 31 December 2005 was approximately RMB1,239.2 million, a substantial increase of 551.9% or RMB1,049.1 million from the balance of RMB190.1 million recorded as at 31 December 2004. Net asset rose to RMB1,873.3 million, an increase of RMB1,151.0 million or 159.3% over the balance as at 31 December 2004 of RMB722.3 million.

#### PLEDGE OF ASSETS

As at 31 December 2005, certain of the Group's property, plant and equipment with an aggregate carrying value of RMB63.6 million, lease prepayments with an aggregate carrying value of RMB9.7 million and investment properties with an aggregate carrying value of RMB5.2 million were pledged to the banks to secure general banking facilities of the Group.

#### USE OF PROCEEDS FROM LISTING AND SUBSEQUENT EVENT

Up to 31 December 2005, the Company has yet to utilise any of the proceeds from the issue of new shares. The proceeds are all deposited with licensed bank in Hong Kong as short term deposits earning interests at rates between 3.7% to 3.8% per annum. There have been no change of intended use of proceeds stated in the IPO prospectus dated 17 November 2005.

The RMB50.0 million deposits paid pursuant to the signing of the PRC preliminary framework agreement dated 23 January 2006, which was duly announced on 25 January 2006 for the possible acquisition of the minority interest in Beijing Parkson, was paid out of the Group's operating cash flow from its PRC operations.

# Total Sales Proceeds And Sales Mix

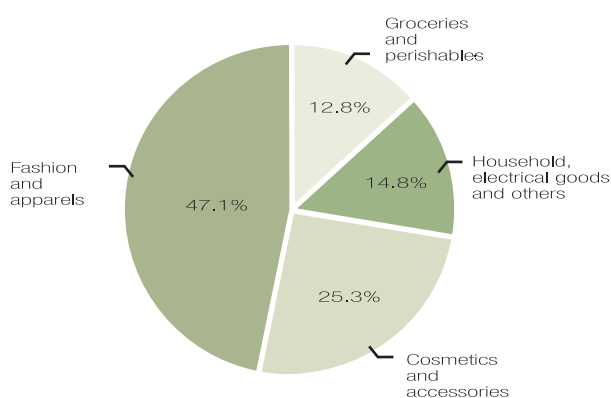
## Total sales proceeds

Year (RMB'000)	2004	2005
Direct sales	292,842	441,220
Concessionaire sales	1,627,924	2,670,785
<b>Total sales proceeds</b>	<b>1,920,766</b>	<b>3,112,005</b>

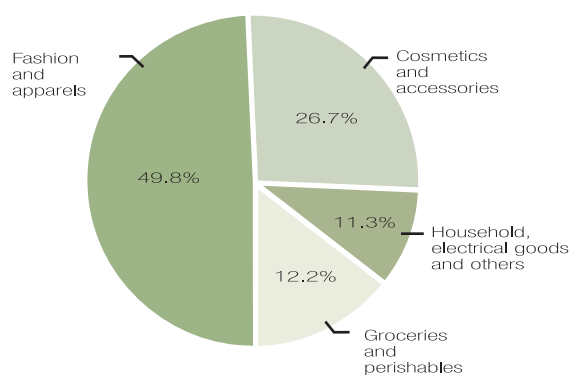
## Sales proceeds by categories

Year (RMB'000)	2004	2005
Fashion and apparels	905,504	1,550,881
Cosmetics and accessories	485,147	830,836
Household, electrical goods and others	283,768	351,068
Groceries and perishables	246,347	379,220
<b>Total sales proceeds</b>	<b>1,920,766</b>	<b>3,112,005</b>

### 2004 Sales Mix



### 2005 Sales Mix



## Segmental information

Over 90% of the Group's revenues and contribution to operating profit is attributable to the operation and management of department stores and all of the Group's turnover and contribution to operating profit is attributable to customers in the PRC. Accordingly no analysis of segment information is presented.

## Employees

As at 31 December 2005, the total number of employees for the Group was approximately 5,000. The Group ensures that all levels of employees are paid competitively by reference to the market and employees are rewarded on performance related basis within the framework of the Group's salary, incentives and bonus scheme.

1,420,000 shares of the Company were subscribed by the employees on a preferential basis at an issue price of HK\$9.80 per share on listing of the Company in November 2005.

No option has been granted since the date of the adoption of employee share option scheme by the Company on 9 November 2005.

## Contingent Liabilities

On 17 February 2005, Beijing Parkson, a jointly-controlled entity of the Group, provided a corporate guarantee of RMB20.0 million (RMB11.2 million attributable to the Group) in favour of a bank in the PRC in respect of a bank loan to China Arts & Crafts (Group) Company.

The underlying loans were due and fully repaid in February 2006.

Save as disclosed above, the Group did not have any significant contingent liabilities as at 31 December 2005.

## Treasury Policies

The Group has limited foreign exchange exposure. More than 95% of the Group's revenue and income are derived in RMB. Hedging instruments including swaps and forwards will be used if necessary to ensure that the Group's exposure to fluctuation of foreign exchange rate is minimised.

The Group maintains a low gearing policy in line with our light asset business model, the balance of bank and other borrowings as at the end of last year was approximately RMB234.3 million serving interest rates ranging from 5.6% to 6.2%. Debt to equity ratio of the Group expressed as a percentage of bank and other borrowings over the total net asset as at 31 December 2005 was approximately 12.5%.