Report of the Directors

The Directors have pleasure in submitting their report and the audited financial statements of the Company and its subsidiaries (the "Group") for the year ended 31 December 2006.

PRINCIPAL ACTIVITIES

The Group is principally engaged in the retailing of electrical appliances and consumer electronics products in the PRC. The Group's revenue is mainly derived from business activities in the PRC. An analysis of the Group's income for the year is set out in note 1 to the financial statements on page 75.

FINANCIAL STATEMENTS

The results of the Group for the year are set out in the Consolidated Income Statement on pages 67 and 68.

The state of affairs of the Group as at 31 December 2006 is set out in the Consolidated Balance Sheet on pages 69 and 70.

The cash flows of the Group for the year are set out in the Consolidated Cash Flow Statement on pages 72 and 73.

SHARE CAPITAL

Details of the movement in share capital of the Company are set out in note 25 to the financial statements on page 130.

DIVIDENDS

An interim dividend of 4.2 HK cents (equivalent to RMB4.3 fen) per ordinary share, amounting to a total of about RMB99,186,000, was paid to the shareholders of the Company during the year.

The Directors recommend a final dividend of 3.6 HK cents (equivalent to RMB3.6 fen) per ordinary share for the year ended 31 December 2006 to be payable to the shareholders whose names appear on the Register of Member of the Company on 16 May 2007. Subject to the approval by the shareholders of the Company of the final dividend recommended by the Directors, the dividends paid and to be paid in respect of the full year 2006 will amount to 7.8 HK cents (equivalent to RMB7.9 fen) per share.

RESERVES

The amounts and particulars of material transfers to and from reserves of the Company and of the Group during the year are set out in note 26 to the financial statements on pages 131 to 133 and in the consolidated statement of changes in equity.

As at 31 December 2006, the Company's reserve available for distribution amounted to RMB175.8 million of which 73.5 million has been proposed as a final dividend for the year.

Report of the Directors

PROPERTY, PLANT AND EQUIPMENT

The movements in property, plant and equipment during the year are set out in note 11 to the financial statements on pages 109 and 110.

MAJOR SUPPLIERS

The percentages of purchases for the year attributable to the Group's major suppliers are as follows:

PURCHASES

– the largest supplier	11.0%
– five largest suppliers combined	30.3%

None of the Directors, their associates or any shareholder (which to the knowledge of the Directors owns more than 5% of the Company's issued share capital) had an interest in the major suppliers noted above.

DONATIONS

During the year, the Group made charitable and other donations totaling approximately RMB0.5 million.

DIRECTORS

The Directors who held office during the year and up to the date of this report were:

EXECUTIVE DIRECTORS

Mr. WONG Kwong Yu
Ms. DU Juan
Mr. LAM Pang
Mr. NG Kin Wah

NON-EXECUTIVE DIRECTOR

Mr. SUN Qiang Chang

INDEPENDENT NON-EXECUTIVE DIRECTORS

Mr. SZE Tsai Ping, Michael
Mr. CHAN Yuk Sang
Mr. Mark Christopher GREAVES
Dr. LIU Peng Hui (appointed on 20 November 2006)

According to the Company's Bye-laws, at each annual general meeting of the Company, one third of the Directors (except the Director holding office as chairman or managing director of the Company) for the time being shall retire from office, and the retiring Directors shall be eligible for re-election. Mr. Lam Pang, Mr. Sze Tsai Ping Michael and Mr. Chan Yuk Sang will retire by rotation at the forthcoming annual general meeting of the Company.

Each of Mr. Sze Tsai Ping, Michael and Mr. Chan Yuk Sang, being eligible, have offered themselves for re-election. Mr. Lam Pang has indicated that he will not offer himself for re-election due to personal reasons. Mr. Lam has confirmed that he has no disagreements with the Board and there is no matter relating to his retirement that will need to be brought to the attention of the shareholders of the Company.

In addition, pursuant to the Company's Bye-laws, any Director appointed either to fill a casual vacancy or as an addition to the Board shall hold office only until the next following annual general meeting of the Company and shall then be eligible for re-election at the meeting (but shall not be taken into account in determining the Directors or the number of Directors who are to retire by rotation at such meeting). Accordingly, the appointment of Dr. Liu Peng Hui will cease at the conclusion of the forthcoming annual general meeting and he, being eligible, will offer himself for re-election.

DIRECTORS' SERVICE CONTRACTS

None of the Directors who are proposed for re-election at the forthcoming annual general meeting of the Company has a service contract with the Company which is not determinable by the Company within one year without payment of compensation (other than statutory compensation).

DIRECTORS' INTERESTS IN CONTRACTS

Apart from the transactions which are disclosed in notes 32 and 38 to the financial statements on page 138, and pages 151 to 153 respectively and in the section headed "Connected Transactions" hereinbelow, there were no other contracts of significance in relation to the Group's business, to which the Company, its holding company, its subsidiaries or fellow subsidiaries was a party and in which a Director of the Company had a material interest, whether directly or indirectly, subsisting at the end of the year or at any time during the year.

DIRECTORS' INTERESTS IN COMPETING BUSINESSES

As at 31 December 2006, the interest of the Directors in businesses (other than those businesses where the Directors were appointed as directors to represent the interests of the Company and/ or any member of the Group) which are considered to compete or are likely to compete, whether directly or indirectly, with the businesses of the Group were as follows:

Name of Director	Name of competing entity	Description of business of competing entity	Nature of interest of the Director
Mr. Wong Kwong Yu	Parent Group	Retail of electrical appliances and consumer electronics products	Beneficial owner
Ms. Du Juan	Parent Group	Retail of electrical appliance and consumer electronics products	Family interest *(Note)*

Note: Ms. Du Juan, spouse of Mr. Wong Kwong Yu, is deemed to be interested in the business of the Parent Group by virtue of her spouse's interest.

During the year, Mr. Wong Kwong Yu and Ms. Du Juan, both executive Directors, have beneficial interest in the Parent Group.

Mr. Wong Kwong Yu and the Company entered into the Non-competition Undertaking on 29 July 2004, pursuant to which Mr. Wong Kwong Yu undertook to the Company that he would not and would procure that the Parent Group would not, among other things, engage in retail sales of electrical appliances and/or consumer electronic products in places in the PRC where the Company had established any retail outlet for the sale of electrical appliances and consumer electronics products under the "GOME Electrical Appliances" trademark, provided that Mr. Wong Kwong Yu remains as the controlling shareholder of the Company. The Company undertook to Mr. Wong Kwong Yu not to directly or indirectly engage in the retail sales of electrical appliances or consumer electronic products in any of the locations in the PRC in which any member of the Parent Group had established, or was as at 3 June 2004 in the course of establishing, any retail outlet for the sale of electrical appliances and consumer electronic products under the "GOME Electrical Appliances" trademark. On 21 July 2006, Mr. Wong Kwong Yu granted a waiver to the Company from its obligations under the Non-competition Undertaking as summarized above in this paragraph in view of the voluntary conditional offer to acquire all shares of China Paradise Electronics Retail Limited.

DIRECTORS' BENEFITS FROM RIGHTS TO ACQUIRE SHARES OR DEBENTURES

At the annual general meeting of the Company held on 15 April 2005, the Company adopted a share option scheme (the "Share Option Scheme") pursuant to which the board of Directors may grant share option to subscribe for the shares of the Company to (inter alia) employees, executives and officers of the Group. No share option has been granted or is outstanding under the Share Option Scheme since its adoption. Save for the Share Option Scheme, the Company has no other share option scheme.

At no time during the year was the Company, any of its holding companies or any of its subsidiaries a party to any arrangements to enable the Directors to acquire benefits by means of acquisition of shares in, or debentures of, the Company or any other body corporate.

DIRECTORS' INTERESTS AND SHORT POSITIONS IN SHARES, UNDERLYING SHARES AND DEBENTURE

As at 31 December 2006, the interests or short positions of the Directors and chief executive of the Company in the shares, underlying shares of equity derivatives and debentures of the Company or any of its associated corporations (within the meaning of Part XV of the Securities and Futures Ordinance ("SFO")) which were recorded in the register required to be kept under Section 352 of the SFO, or which were notified to the Company and The Stock Exchange of Hong Kong Limited (the "Stock Exchange") pursuant to the Model Code for Securities Transactions by Directors of Listed Issuers adopted by the Company were as follows:

LONG POSITIONS IN THE SHARES OF THE COMPANY

	Number of ordinary shares held					
Name of director	**Personal interests**	**Interest of spouse**	**Corporate interests**	**Total**	**Type of interest**	**Approximate % of shareholding as at 31 December 2006**
Wong Kwong Yu	900,087	280,000 *(Note 2)*	1,563,766,947 *(Note 1)*	1,564,947,034	Beneficial owner	51.40%
Du Juan	–	1,564,667,034 *(Note 1)*	280,000 *(Note 2)*	1,564,947,034	Beneficial owner	51.40%

Notes:

1. These shares are held as to 1,377,729,553 shares by Shining Crown Holdings Inc. and as to 186,037,394 shares by Shine Group Limited. Both companies are 100% beneficially owned by Mr. Wong Kwong Yu, the spouse of Ms. Du Juan.

2. These shares are held by Smart Captain Holdings Limited which is 100% beneficially owned by Ms. Du Juan, the spouse of Mr. Wong Kwong Yu.

Report of the Directors

Save as disclosed above, as at 31 December 2006, none of the Company's directors, chief executives or their respective associates had any other interests or short positions in the shares, underlying shares or debentures of the Company or any of its associated corporations (within the meaning of Part XV of the SFO) as recorded in the register required to be kept under Section 352 of the SFO or as otherwise notified to the Company and the Stock Exchange pursuant to the Model Code.

INTERESTS AND SHORT POSITIONS OF SUBSTANTIAL SHAREHOLDERS

So far as is known to any Director or chief executive of the Company, as at 31 December 2006, persons (other than Directors or chief executive of the Company as disclosed above) who had interest or short positions in the shares or underlying shares of equity derivatives of the Company which would fall to be disclosed to the Company under the provisions of Divisions 2 and 3 of Part XV of the SFO or which were recorded in the register required to be kept under Section 336 of the SFO were as follows:

Name of Shareholder	Nature	Number of ordinary shares held	Approximate % of shareholding as at 31 December 2006
Retail Management Company Limited *(Note 1)*	Long position	398,617,648	13.13%
	Short position	30,504,797	1%
Warburg Pincus & Co. *(Note 2)*	Long position	176,680,630	7.71%
Warburg Pincus Partners LLC *(Note 2)*	Long position	176,680,630	7.71%
Warburg Pincus IX LLC *(Note 2)*	Long position	176,680,630	7.71%
Warburg Pincus Private Equity IX, L.P. *(Note 2)*	Long position	176,680,630	7.71%
Real Success International Limited *(Note 2)*	Long position	151,496,788	6.61%
Morgan Stanley *(Note 3)*	Long position	223,591,094	7.34%
	Short position	78,782,678	2.59%
JPMorgan Chase & Co. *(Note 4)*	Long position	184,402,314	6.06%
	Lending pool	122,661,314	4.03%

Notes:

1. To the best knowledge of the Directors, Retail Management Company Limited is majority owned and controlled by Mr. Chen Xiao, President of the Company.

2. Warburg Pincus Private Equity IX, L.P is part of the Warburg Pincus Funds. The general partner of the Warburg Pincus Funds is Warburg Pincus Partners LCC, which is a subsidiary of Warburg Pincus & Co.. Each of Warburg Pincus Partner LLC and Warburg Pincus & Co. is therefore deemed to be interested in the shares held by the Warburg Pincus Funds, which includes Warburg Pincus IX LLC, Warburg Pincus Private Equity IX, L.P.. These are derivative interests and are held as to 151,496,788 Shares by Real Success International Limited and as to 25,183,842 Shares by Sound Idea International Limited, both of which are wholly-owned subsidiaries of Warburg Pincus Private Equity IX, L.P.

3. Morgan Stanley was interested in these shares through its interests in controlled corporations. Of these shares, long position in 134,928,371 shares were held by Morgan Stanley Investment Management Company, long position in 807,000 shares and short position in 807,000 shares were held by MSDW Equity Financing Services (Luxembourg) S.a.r.l., long position in 9,045 shares and short position in 35,000 shares were held by Morgan Stanley Dean Witter Hong Kong Securities Limited, long position in 23,182,414 shares and short position in 20,050,201 shares were held by Morgan Stanley & Co International Limited, long position in 6,657,000 shares were held by Morgan Stanley Asset & Investment Trust Management Co., Limited, long position in 9,109,621 shares and short position in 9,109,621 shares were held by MSDW Equity Finance Services I (Cayman) Limited, long position in 48,764,347 shares and short position in 48,764,347 shares were held by Morgan Stanley & Co. Incorporated and long position in 133,296 shares and short position in 45,259 shares were held by Morgan Stanley Capital Services Inc., all of which are either controlled or indirectly controlled corporations of Morgan Stanley.

4. JPMorgan Chase & Co. was interested in 1,490,000 shares, 60,251,000 shares and 122,661,314 shares in its capacity as beneficial owner, investment manager and custodian corporation/approved lending agent, respectively. JPMorgan Chase Co was interested in such shares through its interests in controlled corporations. Of these shares, 124,884,314 shares were held by JPMorgan Chase Bank, N.A., 12,449,000 shares were held by J.P. Morgan Investment Management Inc., 42,033,000 shares were held by JPMorgan Asset Management (UK) Limited, 1,054,000 shares were held by JPMorgan Asset Management (Canada) Inc., 1,490,000 shares were held by J.P Morgan Whitefriars Inc., and 2,492,000 shares were held by JPMorgan Asset Management (Japan) Limited, all of which are either controlled or indirectly controlled corporations of JPMorgan Chase & Co.

Report of the Directors

As at 31 December 2006, there was no other person (other than the Directors and the chief executive of the Company), who had an interest or short position in the shares or underlying shares of equity derivatives of the Company which would fall to be disclosed to the Company under the provisions of Divisions 2 and 3 of Part XV of the SFO, or who were recorded in the register to be kept by the Company under Section 336 of the SFO, or as otherwise notified to the Company and the Stock Exchange.

SUBSIDIARIES

Details of the Company's principal subsidiaries at 31 December 2006 are set out in note 17 to the financial statements on pages 117 to 123.

CONNECTED TRANSACTIONS

During the year, the Group entered into the following transactions and arrangements with connected persons (as defined in the Listing Rules) of the Company:

(1) On 29 March 2006, the Company entered into an acquisition agreement (the "Acquisition Agreement") with GOME Holdings Limited ("GHL") and Mr. Wong Kwong Yu ("Mr. Wong"), the Chairman of the Board, executive Director and controlling shareholder of the Company, in relation to the acquisition of (a) the entire issued share capital of Grand Hope Investment Limited ("Grand Hope") which in turn holds 35% equity interest in 國美電器有限公司 (GOME Appliance Co., Ltd.) ("GOME Appliance"), and (b) the shareholder's loans in the amount of approximately HK$225.01 million due from Grand Hope to GHL at an aggregate consideration of HK$6,986.70 million, which was satisfied by way of the following: (i) as to approximately HK$5,235.30 million by the issue of shares in the Company ("Shares") to GHL or its nominee at an issue price of HK$8.05 per Share; (ii) as to approximately HK$761.40 million by the set-off against the consideration in the amount of HK$761,426,400.39 payable by Kashmac International Limited, a company wholly-owned by Mr. Wong, to the Company in connection with the disposal of the entire issued share capital of and shareholders' loan due from each of Artway Development Limited and Bestly Legend Limited (which in turn holds a parcel of land located at Area No.7, Xi Ba He Bei Lane, Chaoyang District, Beijing, the PRC by the Company to Kashmac International Limited pursuant to an agreement dated 5 November 2005 entered into between the Company, Mr. Wong and Kashmac International Limited; and (iii) as to HK$990.00 million in cash. Completion of the transactions contemplated under the Acquisition Agreement took place on 8 May 2006.

(2) The Group sells electrical appliances and consumer electronic products to the Parent Group (as defined in note 38 to financial statements on page 151) from time to time on an at-cost basis for a term of three financial years ended 31 December 2007, subject to the annual caps of HK$400.00 million (excluding value added tax), HK$500.00 million (excluding value added tax) and HK$550.00 million (excluding value added tax) for each of the three years ending 31 December 2007 respectively, pursuant to a conditional supply agreement entered into between GOME Appliance, a subsidiary of the Company, and Beijing GOME, a member of the Parent Group, on 17 March 2005. During the year, the total amount of sales made under the aforesaid agreement was about RMB8.59 million (about HK$8.38 million).

(3) The Group purchases electrical appliances and consumer electronic products from Beijing GOME from time to time on an at-cost basis for a term of three financial years ending 31 December 2007, subject to the annual caps of HK$400.00 million (excluding value added tax), HK$500.00 million (excluding value added tax) and HK$550.00 million (excluding value added tax) for each of the three years ending 31 December 2007 respectively, pursuant to a conditional purchase agreement entered into between GOME Appliance and Beijing GOME on 17 March 2005. During the year, the total amount of purchases made under the aforesaid agreement was about RMB237.16 million (about HK$231.39 million).

(4) The Group negotiated with various suppliers for both the Group and the Parent Group on a centralized basis to benefit from the volume purchases and to secure more favourable terms with suppliers. The Group provided purchasing services to the Parent Group (other than GOME Home Appliances H.K. Limited ("Hong Kong GOME")), and charged the Parent Group a fee at the rate of 0.9% of the revenue generated from the sales of the Parent Group (other than Hong Kong GOME) which was determined with reference to the gross profit margin of the Parent Group pursuant to a purchasing service agreement (the "Purchasing Service Agreement") dated 29 July 2004 entered into between 天津國美物流有限公司 (Tianjin Gome Logistics Company Limited) ("Tianjin Logistics"), a subsidiary of the Company, and Beijing Gome. The caps for the purchasing service fee for each of the three years ended 31 December 2006 were RMB55.00 million, RMB85.00 million and RMB125.00 million, respectively. On 4 December 2006, Tianjin Logistics entered into a supplemental agreement to the Purchasing Service Agreement with Beijing Gome, pursuant to which the Purchasing Service Agreement was supplemented by the following: (i) Tianjin Gome may nominate any member of the Group to provide the purchasing service and/or receive the fees payable under the Purchasing Service Agreement; (ii) the term of the Purchasing Service Agreement has been extended to 31 December 2009 unless and until being terminated by either party by giving prior written notice of not less than 60 days to the other; and (iii) the maximum fees to be receivable by Tianjin Logistics or its nominee from Beijing Gome under the Purchasing Service Agreement shall not exceed RMB150 million (excluding value added tax) in each financial year). The purchasing service fees charged during the year was about RMB118.04 million.

(5) The Parent Group is managed by the same management team of the Group for systematic brand building, enhanced market information and optimizing the use of resources in the PRC and Hong Kong. The Group will charge the Parent Group at the rate of 0.75% of the total revenue of the Parent Group if the revenue is equal to or less than RMB5.0 billion or at the rate of 0.6% if the revenue exceeds RMB5.0 billion, which is determined with reference to the expected expenses of the head office level to be allocated to the Parent Group and the expected revenue to be generated from the Parent Group based on the anticipated business growth, pursuant to a management agreement (the "Management Agreement") dated 29 July 2004 entered into between 天津國美商業管理咨詢有限公司 (Tianjin Gome Commercial Consultancy Company Limited) ("Tianjin Consultancy"), a subsidiary of the Company, and Beijing Gome. The caps of the management fees for each of the three years ended 31 December 2006 were RMB43.0 million, RMB65.0 million and RMB101.0 million, respectively. On 4 December 2006, Tianjin Consultancy entered into a supplemental agreement to the Management Agreement with Beijing Gome, pursuant to which the Management Agreement was supplemented by the following: (i) Tianjin Consultancy may nominate any member of the Group to provide the management service and/or receive the fees payable under the Management Agreement; (ii) the term of the Management Agreement has been extended to 31 December 2009 unless and until being terminated by either party by giving prior written notice of not less than 60 days to the other; and (iii) the maximum fees to be receivable by Tianjin Consultancy or its nominee from Beijing Gome under the Management Agreement shall not exceed RMB100.0 million (excluding value added tax) in each financial year). The management fees charged during the year was about RMB84.43 million.

(6) The Parent Group has set up counters in retail outlets operated by the Group for selling audio and visual products. The Parent Group has entered into sub-lease agreement with each of the individual outlets of the Group. According to the sub-lease agreements, the rent is charged at (1) approximately RMB12 per square meter per day; and (2) 5.0% of the total revenue generated from sales of the audio and visual products of the Parent Group. The caps of the sub-lease agreements for each of the three years ended 31 December 2006 were RMB50.0 million, RMB115.0 million and RMB140.0 million, respectively. The total sub-lease income charged for the year was about RMB39.97 million.

All independent non-executive Directors have reviewed the continuing connected transactions as set out paragraphs (2) to (6) above (the "Continuing Connected Transactions") and confirmed that they were entered into:

1. in the ordinary and usual course of business of the Group;

2. either on normal commercial terms or on terms no less favourable to the Group than those available to or from independent third parties; and

3. in accordance with the relevant agreement(s) governing the above-mentioned continuing connected transactions on terms that are fair and reasonable and in the interests of the shareholders of the Company as a whole.

Furthermore, the auditors of the Company have confirmed to the board of Directors that the Continuing Connected Transactions:

1. have been approved by the board of Directors;

2. have not exceed the respective caps stated in the relevant announcements;

3. have been entered into in accordance with the terms of the relevant agreements governing such transactions; and

4. are in accordance with the pricing policies of the Group where such transactions involved the provision of goods or services by the Group.

EMPLOYEE AND REMUNERATION POLICY

As at 31 December 2006, the Group employed a total of 37,781 employees. The Group recruits and promotes individuals based on merit and their development potentials. Remuneration package offered to all employees including Directors is determined with reference to their performance and the prevailing salary levels in the market.

COMMITMENTS

Details of commitments are set out in note 37 to the financial statements on pages 149 and 151.

INDEPENDENCE CONFIRMATION

The Company has received from each of the independent non-executive Directors a confirmation of independence pursuant to Rule 3.13 of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the "Listing Rules"). The board of Directors is satisfied with the independence of each of the independent non-executive Directors.

Report of the Directors

CORPORATE GOVERNANCE

The Company is committed to maintaining a high standard of corporate governance and has complied with the Code on Corporate Governance Practices as set out in Appendix 14 to the Listing Rules. Further information on the Company's corporate governance practices is set out in the Corporate Governance Report on pages 53 to 64.

EXCHANGE RATES EXPOSURE

Details of the exchange rates exposure are set out in note 39 to the financial statements on page 154.

PURCHASE, SALE AND REDEMPTION OF SHARES

During the year ended 31 December 2006, the Company had not redeemed and neither the Company nor any of its subsidiaries had purchased or sold any of the Company's listed securities.

POST BALANCE SHEET EVENTS

Details of the post balance sheet events are set out in note 40 to the financial statements on page 155.

FIVE YEARS FINANCIAL SUMMARY

A summary of the results, assets and liabilities of the Group for the past five years is set out on page 156.

SUFFICIENCY OF PUBLIC FLOAT

The Company has maintained a sufficient public float throughout the year.

AUDITORS

Ernst & Young retire and, being eligible, offer themselves for re-appointment. A resolution for the re-appointment of Ernst & Young as auditors of the Company will be proposed at the forthcoming Annual General Meeting.

On behalf of the Board

Du Juan
Executive Director

Hong Kong, 17 April 2007