

Management Discussion And Analysis

Total gross sales proceeds and operating revenues

During the year under review, the Group generated a total gross sales proceeds received or receivable of RMB6,168.7 million (comprises direct sales, sales proceeds from concessionaire sales, rental incomes, consultancy and management service fees and other operating revenues). Total gross sales proceeds for the year represent a growth of 86.5% or RMB2,860.7 million from RMB3,308.0 million reported in the same period of last year largely as a result of i) the strong SSS growth of approximately 17.1% ii) full year sales contribution from new stores opened last year (the "New Stores") and Parkson branded managed stores acquired throughout the second half of last year (the "Acquired Group") and iii) the inclusion into this year's accounts, the post acquisition sales performances of the 44% Beijing Parkson and the Kunming Stores. The growth was also partly contributed by the receipt of the PRC government's incentive for dividend reinvested to acquire the 44% Beijing Parkson and the change of arrangement with the concessionaires which resulted in increase recognition of other operating revenues. The growth was however partially offset by the reduction in the consultancy and management service fees due to lesser managed stores within the Group's portfolio after the acquisition of some of the managed stores.

The Group generated total merchandise sales of approximately RMB5,769.9 million. The concessionaire sales contributed approximately 86.9% and the direct sales contributed the balance of 13.1%. The Fashion & Apparel category made up approximately 50.0% of the total merchandise sales, the Cosmetics & Accessories category contributed approximately 28.5%, the Household & Electrical category contributed approximately 9.5% and the balance of approximately 12.0% came from the Groceries and Perishables category.

Commission rate from concessionaire sales was within management's expectation at 20.5%. It was 1.1% lower than the previous year due to the lower commission rate for (i) the New Stores and the Acquired Group and (ii) the Kunming Stores.

Total operating revenues of the Group for the year under review grew by RMB969.4 million to RMB2,184.0 million or 79.8% from the numbers reported in the same period of last year. The strong growth rate was in line with the growth of the total gross sales proceeds and partially offset by the reduction of the consultancy and management service fees.



Total Sales Proceeds And Sales Mix

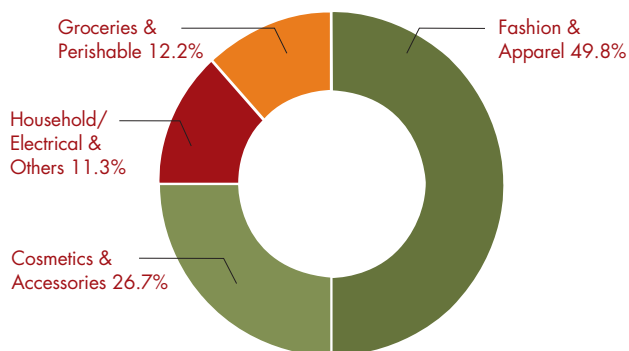
Total sales proceeds

Year (RMB'000)	2005	2006
Direct sales	441,220	758,049
Concessionaire sales	2,670,785	5,011,806
Total sales proceeds.....	<u>3,112,005</u>	<u>5,769,855</u>

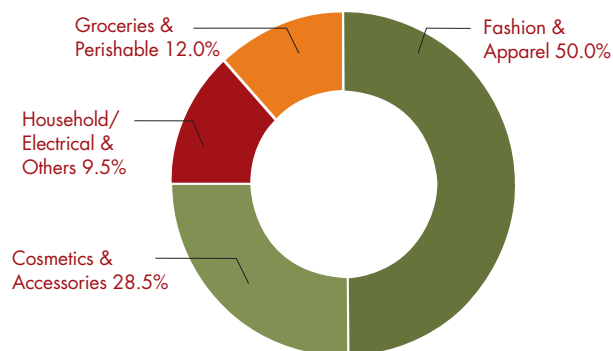
Sales proceeds by categories

Year (RMB'000)	2005	2006
Fashion and apparels	1,550,881	2,884,095
Cosmetics and accessories	830,836	1,645,860
Household, electrical goods and others	351,068	549,098
Groceries and perishables	379,220	690,802
Total sales proceeds	<u>3,112,005</u>	<u>5,769,855</u>

2005 Sales Mix



2006 Sales Mix





Management Discussion And Analysis

Operating Expenses

PURCHASE OF GOODS AND CHANGES IN INVENTORIES

The purchase of goods and changes in inventories refer to the cost of sales for the direct sales. In line with the increase of direct sales, the cost of sales increased to RMB632.3 million, an increase of RMB268.8 million or 74.0% from RMB363.5 million recorded for the same period of last year. The gross profit margin of 16.6% declined marginally by 1.0% from 17.6% recorded for the same period of last year due to the lower gross profit margin of the New Stores, the Acquired Group and the Kunming Stores.

STAFF COSTS

Staff costs increased by RMB76.3 million or 63.4% to RMB196.6 million, the increase was largely contributed by (i) the full year staff cost of the Acquired Group, (ii) the full year staff cost of the New Stores and (iii) the additional staff cost from the 44% Beijing Parkson and Kunming Stores acquisition.

As a percentage to total operating revenues, the staff cost decreased marginally by 0.9% due to improved operating efficiency.

DEPRECIATION AND AMORTISATION

Depreciation and amortisation increased by RMB24.7 million or 38.5% to RMB88.7 million, the increase was largely contributed by (i) the full year depreciation and amortisation cost of the Acquired Group, (ii) the full year depreciation and amortisation cost of New Stores and (iii) the additional depreciation and amortisation cost from the 44% Beijing Parkson and Kunming Stores acquisition.

As a percentage to total operating revenues, depreciation and amortisation cost dropped to 4.1% from 5.3% reported for the same period of last year. The drop is due to the strong increase of the same stores operating revenues and full year operating revenues contribution from New Stores and Acquired Group which are all on long leases and have no building cost and land use rights subject to depreciation and amortisation.



RENTAL EXPENSES

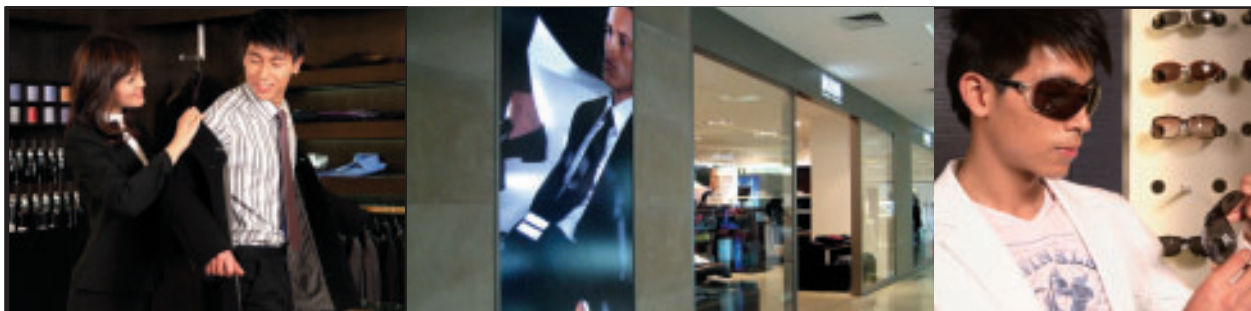
Rental expenses increased by RMB123.2 million or 118.5% to RMB227.1 million. The increase was largely due to the inclusion of i) the full year rental cost for the New Stores and the Acquired Group and ii) additional rental cost from the 44% Beijing Parkson and Kunming Stores acquisition. The increase was also partly due to the increase payment of contingent rent for the performance related lease agreements.

As a percentage to total operating revenues, the rental expenses rose to 10.4%, moved up 1.8% from the same period of last year due largely to the inclusion of full year rental expenses for the New Stores and Acquired Group which are all on long leases as compared to the year 2005 where a substantial portion of the operating revenues recorded were derived from the stores that own the property and there were no related rental expenses.

OTHER OPERATING EXPENSES

Other operating expenses which consist of mainly the utilities cost, marketing and promotional cost, credit card handling expenses, property management cost and general administrative cost increased by RMB165.7 million or 99.9% to RMB331.4 million. Included in the other operating expenses are the exchange loss of approximately RMB13.3 million and the change of arrangement with the concessionaires which resulted in the increase recognition of the operating expenses incurred in direct relation to the increase in other operating revenues recognised. Other than that the increase was generally in line with the improved revenues.

As a percentage to operating revenues, other operating expenses ratio was 15.2%, increased by 1.5%, the increase was mainly due to the factors highlighted in the previous paragraph. The increase was also partly due to the inclusion of full year operating results for the Acquired Group and the New Stores and the heavy promotion cost incurred during the second half of the year 2006.



PROFIT FROM OPERATIONS

Profit from operations increased to RMB707.9 million, an improvement of RMB310.7 million or 78.2%, generally in line with the growth of operating revenues. Profit from operations as a percentage to operating revenues decreased marginally to 32.4% from 32.7% recorded in the same period of last year due to the inclusion of full year performance of the New Stores and the Acquired Group which have lower operating efficiency.



FINANCE INCOME

Finance income, which comprises interest income net of interest expenses increased to RMB23.5 million, an increase of RMB15.1 million or 178.7% from RMB8.4 million recorded for the same period of last year due to the increase interest incomes from the placement of deposits with licensed banks and the interest incomes from the CLN. The increase in interest incomes was however partially offset by the increase of interest expenses in relation to the High Yield Bond and the Commercial Loans.



SHARE OF PROFIT FROM AN ASSOCIATE

This is the share of profit from Shanghai Nine Sea Lion Properties Management Co. Ltd ("Shanghai Lion Property"), an associate of the Company, the share of profit grew from RMB522,000 in 2005 to RMB538,000 in 2006, an increase of RMB16,000 or 3.1%.



INCOME TAX

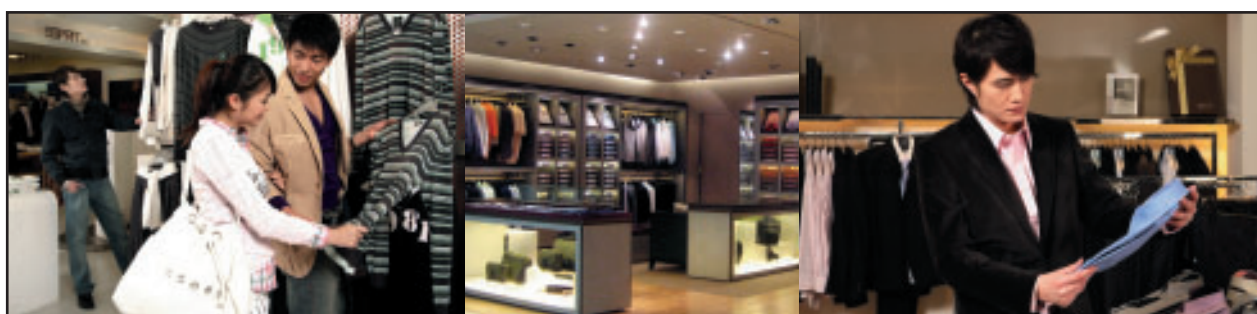
The Group's income tax expense increased by RMB87.0 million or 66.0% to RMB218.8 million in line with the increase in profit from operations. The increase was however partly offset by the lower effective tax rate of 29.9%, a decline of 2.6% from 32.5% recorded for the same period of last year due to the inclusion of higher amount of non taxable interest income and increase number of stores with preferential tax rate.

NET PROFIT FOR THE YEAR

In line with the increase in revenue, the net profit for the year increased to RMB513.2 million, an improvement of RMB238.8 million or 87.1%. The net profit margin improved to 23.5% from 22.6% recorded in the same period of last year due to the lower effective tax rate, growth of operating revenues and the improved operating efficiency.

PROFIT ATTRIBUTABLE TO THE GROUP

Profit attributable to the Group increased to RMB460.8 million, an increase of RMB212.7 million or 85.8%. This is in line with the increase in operating revenues and the profit from operations.



PROFIT ATTRIBUTABLE TO MINORITY INTERESTS

Profit attributable to minority interests increased by RMB26.1 million or 99.1% to RMB52.4 million due to the increase of net profit for the year and the inclusion of full year net profits from stores within the Acquired Group that have higher percentage of minority interest.

LIQUIDITY AND FINANCIAL RESOURCES

The Group's cash and bank balance increase to RMB3,271.4 million, an increase of RMB1,191.0 million from the balance recorded as at the end of December 2005. The increase is largely due to (i) positive cash flow of RMB866.1 million generated from the operating activities, (ii) RMB1,500.0 million that the Group received from the Structure Financing. The increase was however partially set off by the payment of the year 2005 final dividends of RMB143.5 million, the payment of the year 2006 interim dividends of RMB82.8 million and the payment of RMB840.6 million for the acquisition of the 44% Beijing Parkson and the Kunming Stores. Total debt to equity ratio of the Group expressed as a percentage of interest bearing loans and other borrowings over the total equity of RMB2,319.5 million was 138.7% as at 31 December 2006. However, after taken into account on the net effect of the Structure Financing (excluding the CLN and the High Yield Notes from the calculation), the debt to equity ratio of the Group as at the end of December 2006 was approximately 72.9%.

NET CURRENT ASSETS AND NET ASSETS

The Group's net current assets as at 31 December 2006 was approximately RMB1,979.1 million, an increase of 59.7% or RMB739.9 million from the balance of RMB1,239.2 million recorded as at 31 December 2005 due largely to the proceeds from the Structure Financing and partially offset by the cash payment made for the 44% Beijing Parkson and Kunming Stores acquisition. Net asset rose to RMB2,319.5 million, an increase of RMB446.2 million or 23.8% over the balance as at 31 December 2005 due largely to the net profit contribution for the year 2006 and the revaluation surplus pursuant to the 44% Beijing Parkson acquisition after offsetting the dividends paid during the year.



PLEDGE OF ASSETS

As at 31 December 2006, certain of the Group's property, plant and equipment with an aggregated carrying value of RMB65.8 million and certain of the Group's lease prepayments with an aggregated carrying value of RMB122.6 million were pledged to the banks to secure general banking facilities of the Group.

Shares in certain subsidiaries of the Company were also pledged pursuant to the Structure Financing.

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 2006, total number of employees for the Group was approximately 5,800. The Group ensures that all levels of employees are paid competitively within the standard in the market and employees are rewarded on performance related basis within the framework of the Group's salary, incentives and bonus scheme.

On 10 January 2007, a total of 8,188,950 share options were granted to 482 eligible employees at an exercise price of Hong Kong Dollars ("HK\$") 36.75 per share pursuant to the share option scheme adopted by the Company on 9 November 2005.

CONTINGENT LIABILITIES

The Group did not have any significant contingent liabilities as at 31 December 2006.

TREASURY POLICIES

The business transactions of the Group were mainly denominated in Renminbi. Therefore, except for the capital market transactions for funding needs, there is limited exposure in foreign exchange risk. Hedging instruments including swaps and forwards have been used in the past and would be used in the future if necessary to minimise the Group's exposure to the foreign exchange rate and the interest rate fluctuation.

In relation to the High Yield Notes issued in November 2006, the Group has simultaneously entered into the Structure Financing arrangement, which include interest rate swaps to eliminate the Group's exposure to exchange rate and interest rate fluctuations. As the result from the use of the interest rate swaps, the Group is now serving a fixed annual interest rate of 7.875% for the High Yield Notes, serving a fixed annual interest rate of 10.30% for the Commercial Loans and receiving a fixed annual interest income at the rate of 9.80% for the CLN. As at 31 December 2006, apart from the Structure Financing, the Group's interest bearing loans were approximately RMB190.9 million serving interest rates between 5.9% to 6.2%.

Debt to equity ratio of the Group expressed as a percentage of interest bearing loans and other borrowings over the total equity was approximately 138.7% as at 31 December 2006. However, after taken into account on the net effect of the Structure Financing, the debt to equity ratio of the Group was approximately 72.9%.

