MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITIONS AND RESULTS OF OPERATIONS

Turnover

Turnover increased from RMB851.7 million in FY2005 to RMB1.055 billion in FY2006, representing an increase of 23.86%. Turnover comprises three different segments: retail, OEM, and other turnover. In FY2006, the retail segment grew in importance in terms of overall turnover, seeing an increase from 75.56% of the total Group turnover in FY2005, to 79.51% of the total Group turnover in FY2006.

Retail

Retail turnover increased from RMB643.5 million in FY2005 to RMB838.8 million in FY2006, representing an increase of 30.34%. The increase was driven by an increase in unit volume sold, growth in sales in existing stores, sales from new stores, and an increase in the average selling price. The increase in unit volume sold is due to, among other factors, the increase in the number of PORTS and BMW LIFESTYLE retail outlets from 325 as at 31 December 2005 to 357 as at 31 December 2006. The number of PORTS stores open as at 31 December 2006 increased by 10.46% over last year. In 2006, the management team concentrated on renovating older locations to bring them in-line with the company's 5th generation store design and limiting new store openings, thereby maintaining the exclusivity of PORTS retail locations, while driving traffic to, and thereby increasing the profitability of the existing PORTS stores. The size of the BMW LIFESTYLE retail store network grew by 29.63% in FY2006 over last year, increasing from 27 stores to 35 stores as at 31 December 2005 and 2006, respectively. The increase in average selling price for both PORTS and BMW LIFESTYLE products reflects, in part, the increasing strength of the PORTS and BMW LIFESTYLE brands, and the effectiveness of the Group's marketing program. The Directors believe that the increase in retail turnover is also partially attributable to the continued growth in the average annual household income in urban cities in the PRC, where most of the Group's retail outlets are located. The increase in household income enables more PRC consumers to purchase the Group's products.

During FY2006, turnover from concessions represented 73.9% of the total retail turnover while turnover from retail stores represented 26.1% of the total retail turnover. Accordingly, sales from concessions in department stores still represented the majority of the Group's retail turnover. However, the Directors believe that retail stores located in upscale shopping malls will become increasingly important to the positioning of the PORTS and BMW LIFESTYLE brands.

As at 31 December 2006, turnover from the retail segment represented a larger percentage of the overall turnover of the Group than in previous years, seeing an increase from 75.56% of the total Group turnover in FY2005, to 79.51% of the total Group turnover in FY2006. However, with the limited number of upscale shopping malls available in the PRC, concessions in department stores will continue to dominate the PORTS and BMW Lifestyle retail store network in terms of importance.

OEM

Turnover from the OEM segment increased slightly from RMB156.9 million in FY2005 to RMB159.8 million in FY2006, representing an increase of 1.81%. Turnover from the OEM segment as a percentage of overall turnover from the Group however, declined from 18.43% in FY2005 to 15.15% in FY2006. This decline was mainly due to the increasing importance of the Retail segment to the overall turnover for the Group, as the Retail segment is experiencing stronger growth than the OEM and "Other" segments. There was also a continuing negative effect on turnover resulting from the safeguard quotas imposed by the EU and the USA in 2005, which affected turnover in the first half of 2006. The turnaround time for orders is approximately 3 months. Although orders from U.S and European customers resumed in January 2006, this turnaround time meant the selling season for OEM business was reduced from 6 to 3 months, reducing turnover for the OEM segment in the first half of 2006 by 50%. The Directors anticipate that the percentage contribution of OEM turnover to the Group's total turnover will continue to decline in 2007.

Other

Other turnover increased by approximately 9.97%, from RMB51.2 million in FY2005 to RMB56.3 million in FY2006. Turnover for the "Other" segment continued to be negatively affected during the first half of 2006 by the imposition of safeguard quotas by the EU governments in 2005, which affected the export of BMW LIFESTLYE products to Europe during the first 3 months of 2006. Although the growth in BMW LIFESTYLE apparel exports from PORTS to BMW AG in Germany was particularly robust during the first half of FY2005, exports from PORTS to BMW AG have been slow to resume in FY2006. The Directors anticipate that the growth rate of exports of BMW LIFESTYLE products will continue to increase through 2008, when quotas are anticipated to be eliminated in accordance with the terms of China's entry into the World Trade Organization ("WTO").

Cost of sales

Cost of sales increased from RMB295.8 million in FY2005 to RMB321.3 million in FY2006, representing an increase of 8.62%. The increase in cost of sales was directly related to the increase in the Group's turnover during FY2006, although the percentage increase in cost of sales is significantly less than the percentage increase in the total turnover and volume of sales.

Gross profit

Gross profit increased from RMB555.9 million in FY2005 to RMB733.6 million in FY2006, representing an increase of 31.97%. Gross profit margin also increased from 65.27% in FY2005 to 69.54% in FY2006. The improvement in gross profit margin was driven predominantly by the increasing contribution of gross profit generated by the retail segment.

Retail

Gross Profit for the retail segment increased from RMB504.9 million in FY2005 to RMB678.5 million in FY2006, representing an increase of 34.38%. Gross profit margin for the retail segment also improved from 78.46% in FY2005 to 80.89% in FY2006. The Directors believe that the gross profit margin enjoyed by the retail segment is in line with the profit margin level achieved by other international high-end fashion and luxury brands. In FY2006, the retail segment accounted for 92.49% of the Group's total gross profit, up from 90.88% of the Group's total gross profit in FY2005. This increase, in part, reflects the growing importance of the retail segment to the Group.

OEM

Gross profit from the OEM segment increased from RMB27.0 million in FY2005 to RMB28.8 million in FY2006, representing an increase of 6.67%. Gross profit margin also improved from 17.20% in FY2005 to 18.01% in FY2006. The increase in gross profit margin is partly the result of the controls imposed by the Group in refusing orders with unacceptable gross profit margin. The Directors are very pleased with the improvement of the gross profit margin. However, as OEM is a very competitive business, the Directors do not expect any further significant improvement in the performance of the OEM segment going forward.

Other

Gross profit from the "Other" segment increased from RMB23.7 million in FY2005 to RMB26.3 million in FY2006, representing an increase of 10.04%. Gross profit margin decreased slightly from 46.71% in FY2005 to 46.70% in FY2006. As a result of the residual negative effects of the European safeguard quotas imposed in the second half of 2005, the "Other" segment was affected in FY2006 by the imposition of safeguard quotas by EU governments. BMW LIFESTYLE products however, have been well received by BMW dealers throughout the world, and the Directors anticipate growth in the export of BMW LIFESTYLE products to resume in 2007.

Other operating income

Other operating income increased from RMB11.4 million in FY2005 to RMB15.4 million in FY2006, representing an increase of 34.84%. This increase was due mainly to increases in royalty income and store design and decoration service income, which increased by 25.51% and 39.77%, respectively. The Directors anticipate that income from store design and decoration services , together with royalty income received from licensees of the PORTS brand name will continue to increase during FY2007.

Operating Expenses

Operating expenses increased from RMB381.3 million in FY2005 to RMB469.0 million in FY2006, representing an increase of 22.99%. Operating expenses have generally increased in accordance with the growth of the business. Expenses consist of distribution expenses, administrative expenses and other operating expenses.

Distribution expenses

Distribution expenses increased from RMB319.8 million in FY2005 to RMB397.8 million in FY2006, representing an increase of 24.39%. The increase was principally due to increases in sales commissions, rental payments, advertising and promotional costs and depreciation charges. Depreciation charges increased from RMB19.0 million in FY2005 to RMB25.6 million in FY2006, representing an increase of 34.65%, as a result of increased investments in manufacturing, distribution facilities and retail outlets. Advertising and promotional costs increased from RMB27.3 million in FY2005 to RMB32.7 million in FY2006, representing an increase of 20.12%, and amounting to approximately 3.90% of FY2006 retail turnover. Rental charges increased from RMB166.7 million in FY2005 to RMB210.2million in FY2006, representing an increase of 26.15%. In FY2006, rental charges represented 25.06% of total retail turnover as compared to 25.90% in FY2005.

Administrative expenses

Administrative expenses remained fairly stable year-on-year, from RMB33.5 million in FY2005 to RMB33.4 million in FY2006, representing a slight decrease of 0.37%.

Other operating expenses

Other operating expenses increased from RMB28.1 million in FY2005 to RMB37.9 million in FY2006, representing an increase of 34.92%. This increase was due to an increase of RMB9.8 million in the provision for ageing inventory.

Profit from operations

As a result of the increase in turnover, and the economies of scale derived from the growth of the Group's operations, the Group's profit from operations increased from RMB186.0 million in FY2005 to RMB280.0 million in FY2006, representing an increase of 50.57%. The Group's operating margin (i.e. profit from operations expressed as a percentage of turnover), increased from 21.83% in FY2005 to 26.54% in FY2006.

Income tax expense

The Group's effective income tax rate increased from 8.93% of profit before tax in FY2005 to 10.32% of profit before tax in FY2006. The tax refund received by the Group increased from RMB7.0 million in FY2005 to RMB9.4 million in FY2006, representing an increase of 33.91%.

Profit attributable to shareholders

As a result of the factors discussed above, the Company's profit attributable to shareholders increased from 165.1 million in FY2005 to RMB254.0 million in FY2006, representing an increase of 53.88%. The Company's net profit margin also improved from 19.38% in FY2005 to 24.08% in FY2006.

Financial Position & Liquidity

The Group continues to enjoy a strong financial position, with significant cash reserves being generated from normal business operations. As at 31 December 2006, the Group had approximately RMB412.7 million in cash, cash equivalents and time deposits, as compared to RMB346.7 million as at 31 December 2005, representing an increase of 19.01%. The Group also had access to significant bank loans and overdraft facilities, although these were not utilized. The Group currently has no interest bearing loans with any commercial banks, and as at 31 December 2006, the Group's gearing ratio was zero. Cash inflow from operating activities increased from RMB126.7 million in FY2005 to RMB221.2 million in FY2006, representing an increase of 74.59%.

Acquisitions & Disposals of Subsidiaries & Associated Companies

The Group did not engage in any acquisitions or disposals of any subsidiaries or associated companies during the 2006 Financial Year.

Currency Risk Management

The Group's cash balances from normal business operations are mainly deposited in Renminbi ("RMB"), United States dollars ("US$"), Hong Kong dollars ("HK$") and the European Union common currency ("Euros"), with major banks in Hong Kong and the PRC. The Group considers its risk exposure to currency fluctuations to be minimal.

Capital Commitments & Contingent Liabilities

As at 31 December 2006, the Group had capital commitments of RMB76.4 million (compared to RMB84.1 million as at 31 December 2005), of which RMB75.0 million was authorized but not contracted for (compared to RMB81.0 million as at 31 December 2005), and RMB1.4 million was authorized and already contracted for (compared to RMB3.1 million as at 31 December 2005). These capital commitments were primarily attributable to planned and budgeted activities such as the opening of superstores, the expansion and renovation of retail outlets and the expansion of manufacturing and distribution facilities. As at 31 December 2006, the Group had no material contingent liabilities.

Capital Structure of the Group

The Group requires working capital to support its manufacturing, retail, OEM and other operations. As at 31 December 2005, the Group had cash, cash equivalents and time deposits of approximately RMB346.7 million, denominated principally in RMB, US$, HK$ and Euros. As at 31 December 2006, cash, cash equivalents and time deposits held by the Group increased to approximately RMB412.7 million, denominated principally in RMB, US$, HK$ and Euros. The Directors believe that the cash balances and net cash inflow from operating activities are sufficient to support the operating activities of the Group.

Major Customers & Suppliers

During FY2006, the Group purchased approximately 16% and 28% of its goods and services from its largest supplier and its five largest suppliers, respectively. The percentages of turnover attributable to the Group's largest customer and its five largest customers combined were roughly 6% and 17%, respectively. None of the Directors, their associates or shareholders (which to the best knowledge of the Directors own more than 5% of the Company's share capital) was interested at any time in the year in the above suppliers or customers.

Charges on Assets

As at 31 December 2006, the Group had not charged any of its assets.

Human Resources

As at 31 December 2006, the Group had approximately 4,860 employees. Total personnel expenses, comprised of wages, salaries, and benefits, amounted to RMB157.2 million in FY2006, compared with RMB107.8 million in FY2005, representing an increase of 45.85%.

The Group is committed to fostering a safe and comfortable workplace and a corporate culture that emphasizes training and career development opportunities and rewards employees for performance. A competitive remuneration scheme, a safe and comfortable work environment, and a merit-based advancement program provide incentives for employees to excel in their areas of responsibility. The multi-cultural environment that exists at the Company also provides a unique opportunity for employees from all over the world to perform and excel in their respective disciplines, while enabling them to exchange knowledge concerning best practices from their own respective cultures. In addition, share options were granted to eligible employees and Directors pursuant to the terms and conditions of the share option scheme adopted by the Company on 14 October 2003. In FY2006 16,000,000 additional shares were granted to eligible employees and Directors under the terms and conditions of the share option scheme.

Post-Balance Sheet Date Events

On 29 December 2006, the Standing Committee of the Tenth NPC passed a resolution to submit the draft corporate income tax law to the Tenth NPC plenary session for voting. According to the income tax law that was passed at the Tenth NPC plenary session on 16 March 2007, the income tax rates that are applicable to certain of the Company's subsidiaries' located in the PRC ("PRC subsidiaries") will be revised. The new law will take effect on 1 January 2008. The Group is in the process of making an assessment of the financial impact of this new tax law on the Group's current and deferred tax position for the year 2007 and the years thereafter.