OVERVIEW

The Group is principally engaged in the design, manufacture and wholesale of a wide range of home furniture products including mainly wood-based furniture and mattresses in the PRC and overseas markets. Banking on its strong capabilities in furniture design and brand management, the Group also derives licensing fees from granting non-exclusive rights to other furniture manufacturers for use of its own brands and product designs.

The Group's home furniture products are principally categorised into the classic furniture series and the modern furniture series targeting at middle and high price point consumers. Products branded under the classic furniture series are generally larger in size and characterised by elaborate and intricate carving and finishing. The products under the following brand names are classified under the classic furniture series:

Brand name	**Target market segment**	**Recommended retail price range** *(approximately RMB per set (Note))*
Johnston (self-manufacture)	[Sophisticated middle and high price point consumers who demand grand and luxurious designs]	[20,000 – 76,000]
New Nobleman (self-manufacture)	[Middle and high price point consumers who have the predilection for Spanish-styled classic furniture]	[19,000 – 26,000]
Classic Sanroy (under licence)	[High price point consumers who demand luxurious furniture products]	[30,000 – 40,000]

Products under the modern furniture series are characterised by simple and trendy designs with minimal use of decorative items, targeted at younger and middle price point consumers who look for trendy, functional and affordable home furniture. The products under the following brand names are classified under the modern furniture series:

Brand name	**Target market segment**	**Recommended retail price range** *(approximately RMB per set (Note))*
PZ-King (self-manufacture)	[Middle price point consumers]	[9,000 – 15,000]
Mandarin (self-manufacture)	[Middle price point consumers who have the preference for Italian-styled modern furniture]	[7,000 – 12,000]
Oriant (under licence)	[Young aged middle price point consumers]	[5,000 – 13,000]

Note: A set of furniture comprises a bed, two bedside cabinets, a wardrobe and a dressing table.

The Group uses its brand "Degas" to market the branded mattresses it manufactures. All the Group's mattresses are for export only.

Brand name	**Target market segment**	**Recommended retail price range** *(approximately HK$ per piece)*
Degas (self-manufacture)	[Middle price point consumers]	[900 – 4,000]

Set out below is a table showing the breakdown of the Group's turnover by business activities and brand names during the Track Record Period:

	For the year ended 31 December					
	2006		2007		2008	
	HK$'000	*%*	*HK$'000*	*%*	*HK$'000*	*%*
Domestic sales						
Johnston	74,921	*20.3*	106,120	*21.5*	128,588	*24.1*
PZ-King	52,764	*14.3*	48,976	*9.9*	54,273	*10.2*
Mandarin	20,745	*5.6*	55,926	*11.4*	51,844	*9.7*
New Nobleman	–	–	–	–	19,382	*3.6*
	148,430	***40.2***	**211,022**	***42.8***	**254,087**	***47.6***
Exports						
Branded						
– Johnston	–	–	36,336	*7.4*	49,101	*9.2*
– PZ-King	45,959	*12.4*	38,003	*7.7*	34,583	*6.5*
Mattress	50,393	*13.6*	58,748	*11.9*	51,665	*9.7*
Unbranded	97,445	*26.4*	120,651	*24.5*	125,963	*23.5*
	193,797	***52.4***	**253,738**	***51.5***	**261,312**	***48.9***
Licensing fees						
Oriant	19,754	*5.3*	23,829	*4.9*	17,546	*3.3*
New Nobleman	–	–	3,141	*0.6*	–	–
Classic Sanroy	1,347	*0.4*	939	*0.2*	1,401	*0.2*
Mandarin	6,298	*1.7*	–	–	–	–
	27,399	***7.4***	**27,909**	***5.7***	**18,947**	***3.5***
Total	**369,626**	***100.0***	**492,669**	***100.0***	**534,346**	***100.0***

During the Track Record Period, sales to the five largest customers accounted for approximately 32.6%, 32.3% and [29.8]% of the total turnover of the Group respectively, whilst the sales contribution from the largest customer to the Group's total turnover were 10.9%, 11.2% and 8.5% respectively. The five largest customers of the Group during the Track Record Period comprised home furniture retailers, importers and a building contractor.

Domestic sales

During the Track Record Period, the Group did not operate any retail shops and relied on domestic distributors to market its furniture products to end-users in the PRC. As at the Latest Practicable Date, the Group contracted with approximately [511] local furniture distributors to market its branded furniture products to end-users in the PRC. Over [75%] of these distributors were operated in the form of sole proprietorship, each operating one to two shops in their respective regions approved by the Group. As at the Latest Practicable Date, these [511] local furniture distributors operated over 600 approved shops covering [22] provinces, [4] municipalities and [4] autonomous regions in the PRC. The number of years of relationship between the Group and these distributors ranged from approximately 1 to 14 years. The Directors confirmed that none of them, the Shareholders who, to the knowledge of the Directors, held 5% or more of the issued share capital of the Company as at the Latest Practicable Date, and the senior management of the Group, or any of their respective associates had any interest in any of the distributors of the Group during the Track Record Period.

The following table sets out the total number of distributors and approved shops in the PRC as at 31 December 2006, 2007 and 2008, and the average annual turnover per approved shop during the Track Record Period:

	As at 31 December		
	2006	**2007**	**2008**
Number of distributors	348	435	[471]
Number of approved shops	380	482	[565]
Average annual turnover per approved shop *(HK$'000)*	390.6	437.8	[449.7]

The relationship between the Group and each of the distributors is governed by a distribution framework agreement, which has a standard term of one year and is subject to renewal by mutual agreement upon expiry. For details of the distribution framework agreement, please refer to the sub-paragraph headed "Distribution framework agreement" in the paragraph headed "Sales and distribution" in the section headed "Business" in this document.

Export sales

During the Track Record Period, the Group participated in various furniture trade shows and exhibitions in the PRC and in Europe. These events are usually attended by furniture manufacturers as well as furniture buyers, such as overseas sourcing companies, furniture importers and retailers. The Group has been able to build up business relationships with a number of these overseas customers through attending trade shows and exhibitions over the years. During the Track Record Period, the Group's overseas customers were mainly furniture retailers and importers. The top five largest customers of the Group during the Track Record Period were mainly furniture retailers and importers in the overseas markets. During the three years ended 31 December 2008, the Group transacted with over 170, 140 and 90 overseas customers respectively for its export business. Set out below is a table showing the breakdown of the Group's export sales by geographical locations during the Track Record Period:

	For the year ended 31 December					
	2006		**2007**		**2008**	
	HK$'000	*%*	*HK$'000*	*%*	*HK$'000*	*%*
Asia *(Note 1)*	127,850	*66.0*	172,942	*68.2*	176,896	*67.7*
Europe *(Note 2)*	24,817	*12.8*	32,287	*12.7*	35,370	*13.5*
Others *(Note 3)*	41,130	*21.2*	48,509	*19.1*	49,046	*18.8*
Total	**193,797**	***100.0***	**253,738**	***100.0***	**261,312**	***100.0***

Notes:

1. Asia mainly represented Japan, Taiwan, Middle East and Southeast Asia.

2. Europe mainly represented Sweden, Italy, Spain and Germany.

3. Others mainly represented the United States, Canada, Angola and Ivory Coast.

As at the Latest Practicable Date, the number of years of relationship between the Group and its overseas customers ranged from [1] to [15] years. The Directors confirmed that none of them, the Shareholders who, to the knowledge of the Directors, held 5% or more of the issued share capital of the Company as at the Latest Practicable Date, and the senior management of the Group, or any of their respective associates had any interest in any of the overseas customers of the Group during the Track Record Period.

Licensing

In addition to its conventional furniture manufacturing and sales business, the Group grants non-exclusive rights to licensees for the use of its certain brand names and product designs in the PRC. During the Track Record Period, the Group received licensing fees amounting to approximately HK$27.4 million, HK$27.9 million, and HK$[18.9] million respectively. Under the licence agreement, the Group is responsible for the nationwide brand promotional activities to boost the market image and brand awareness of the products under the licence. For details of the licence agreement, please refer to the sub-paragraph headed "Licence agreement" in the paragraph headed "Licensing arrangements" in the section headed "Business" in this document.

The customers of licensees are mainly furniture distributors in the PRC. As at the Latest Practicable Date, the number of years of business relationship between the Group and the licensees ranged from [1] to [13] years. The Directors confirmed that none of them, the Shareholders who, to the knowledge of the Directors, held 5% or more of the issued share capital of the Company as at the Latest Practicable Date, and the senior management of the Group, or any of their respective associates had any interest in any of these furniture manufacturers during the Track Record Period.

Procurement and outsourcing

During the Track Record Period, the Group had over [270], [250] and [180] suppliers respectively and the five largest suppliers included suppliers of raw materials and contract manufacturers who handled outsourced manufacturing of certain furniture products. Purchases from the Group's five largest suppliers in aggregate represented approximately 27.7%, 41.5% and 49.8% of the Group's total purchases and purchases from the largest supplier of the Group accounted for approximately 9.7%, 14.6% and 14.4% of the Group's total purchases for the three years ended 31 December 2008 respectively.

In addition to purchases from its raw material suppliers, the Group makes purchases of finished products from contract manufacturers by way of outsourcing the production of certain furniture products with simple designs and minimal decorative features or on the occasions when its production capacity is running close to full utilisation. During the Track Record Period, the Group engaged 16, 11 and [7] contract manufacturers in the PRC respectively to handle the outsourced manufacturing. The Directors confirmed that none of them, the Shareholders who, to the knowledge of the Directors, held 5% or more of the issued share capital of the Company as at the Latest Practicable Date, and the senior management of the Group, or any of their respective associates had any interest in any of the raw material suppliers and contract manufacturers during the Track Record Period.

Production facilities

The Group's furniture production facilities are located at Shenzhen and Dongguan, Guangdong Province, the PRC. For details of the Group's production facilities, please refer to the sub-paragraph headed "Production facilities" in the paragraph headed "Production" in the section headed "Business" in the document.

With the intention to increase its production capacity for its modern furniture series and the "CHINATAG" furniture products, which are expected to launch in [2010], the Group is presently constructing new production facilities, Shenzhen Xingli Production Base, on Longgang Land I it acquired in June 2007. The Group has planned to invest approximately RMB[121.2] million (approximately HK$136.0 million) for the development of the Shenzhen Xingli Production Base.

With a gross floor area of approximately 38,869 sq.m., the construction of the Shenzhen Xingli Production Base is expected to complete in June 2009. The Group expects to commence the trial production in August 2009 and the full scale production in November 2009. Upon its full scale production, the new production facilities at the Shenzhen Xingli Production Base are expected to provide an annual production capacity of approximately 31,800 furniture sets. The Directors consider that the completion of Shenzhen Xingli Production Base would have positive impact on the Group's profitability as the new production base would enable the Group to expand its production capacities and to capture the growing business opportunities brought about by the expansion of the PRC furniture industry.

Ownership of the Group

During the Track Record Period, the Group experienced a change in controlling shareholder. Since its incorporation in April 2004 and up to November 2004, the Company was all along jointly controlled by the four Founders or their respective investment vehicles. In August 2004, the investment vehicles of the Founders entered into an agreement with Talent Sino Holdings Limited, a wholly-owned subsidiary of Omnicorp Limited, for the acquisition by the latter of approximately 51.52% of the enlarged issued share capital of the Company. In July 2006, Mr. Fang Shin, who was then holding approximately 2.7% interest in Omnicorp Limited, through his investment vehicle, namely Triple Express, acquired from Talent Sino Holdings Limited its entire interest in the Company together with a shareholder's loan owed by the Company to Talent Sino Holdings Limited.

Despite the change in the controlling shareholder of the Company when Omnicorp Limited disposed of its entire interest in the Company to Mr. Fang Shin in July 2006, the Group's management and business operations were not affected and remained stable throughout the Track Record Period. During the period when Omnicorp Limited was the controlling shareholder of the Company, the Group's management and the daily operations were entirely in the hands of the Founders. None of the Directors nominated by Omnicorp Limited assumed any management role or participated in the day to day operation of the Company and their directorships were merely reflective of the majority shareholding in the Company. Omnicorp Limited only seconded to the Company an accountant to monitor the Group's financial reporting from November 2004 to July 2006. Like Omnicorp Limited, Mr. Fang Shin saw his acquisition of the interest in the Company as an investment and had no intention to take part in its management. Mr. Fang Shin had been a Director since July 2006 and he also nominated his son, Mr. Fang Yan Zau, Alexander, to be a member of the Board as well. Mr. Fang Shin resigned as a Director effective on [29 May] 2009. The Board [was] restructured to consist of two executive Directors, namely Mr. Sung and Mr. Cheung, one non-executive Director, Mr. Fang Yan Zau, Alexander, and three independent non-executive Directors [prior to] [●].

Non-compliance issues

As a result of its rapid expansion during the Track Record Period, the Group has inadvertently failed to comply with certain laws, rules and regulations of the PRC and Hong Kong. Summarised below are the Group's incidents of non-compliance during the Track Record Period:

(i) failure to obtain the environmental protection facilities approval for the production facilities prior to the commencement of operations of Shenzhen Xingli and Dongguan Super Furniture;

(ii) failure to make timely housing provident fund contributions by Shenzhen Xingli, Shenzhen Xingli Zundian and Dongguan Super Furniture and failure to make employee social insurances contributions by Dongguan Super Furniture;

(iii) late filings of the Company's subsidiaries in accordance with the Companies Ordinance and Business Registration Ordinance; and

(iv) failure to notify the IRD by Hing Lee Furniture of its chargeability to tax within the prescribed time frame.

For further details of these non-compliance incidents and the remedial actions taken by the Group to rectify these incidents, please refer to [the paragraph headed "Compliance and litigation" in the section headed "Business" in this document]. The Directors believe that, given the remedial actions the Group has taken, none of these non-compliance incidents would give rise to any material adverse impact on the Group's operation.

Furthermore, in view of the occurrence of the above mentioned non-compliance incidents, in December 2008, the Group has set up a compliance department, headed by the chief financial officer and staffed by a qualified accountant and an internal audit manager, to ensure that the Group's operations are in compliance with applicable laws, rules and regulations, to strengthen its existing internal control framework, to recommend best practices for corporate governance and to report internal control deficiencies as well as remedial plans from time to time.

Indemnities

Pursuant to the Deed of Indemnity, each of the Founders and their respective investment vehicles has jointly and severally agreed with and undertaken to the Company (for itself and as trustee for other members of the Group) that he/it will fully indemnify the Group and each member of the Group and at all times keep them and each of them fully indemnified from and against all claims, damages, fines, penalties, loss, payments, liabilities, costs and expenses which any member of the Group may incur, suffer and accrue, directly or indirectly, from or in connection with, any failure, delay or defects of corporate or regulatory compliance as mentioned above on or before the date on which [●] save for those already provided by the Group in its accounts.

COMPETITIVE STRENGTHS

The Directors consider that the Group's competitive edges lie in the following areas:

- Commitment in product design and development and innovation
- Comprehensive product range
- Well-established and strong brand names
- Extensive distribution network
- Established long-term relationships with distributors
- Experienced and capable management team

STRATEGIES

The Directors believe that there are promising prospects in the home furniture industry in the PRC. In order to further expand its business, the Group intends to adopt the following strategies:

- Increasing brand recognition and enhancing corporate profile

  The Group intends to strengthen public awareness of its brands, in particular, "Johnston", "Oriant", "PZ-King" and "CHINATAG", as well as to enhance corporate profile through employing multi-faceted advertising strategies.

- Strengthening design and development capabilities and expanding product range

  The Group plans to strengthen its design and development capabilities through the deployment of advanced design technology and equipment, recruitment of additional four to five designers from domestic leading design institutes in 2010 and provision of continuous training to its design and development staff. The Group also plans to set up a testing centre for testing newly designed products, raw materials used in production and finished products.

- Increasing market penetration in the PRC

  The Directors believe that there is substantial growth potential for the home furniture industry in the PRC. Therefore, the Group will put more efforts in marketing activities and customer service support to enhance its market penetration and expand the distribution network of the Group's branded furniture products in the PRC.

- Increasing production capacity and improving production efficiency by deployment of new production equipment

  In view of the continuous growth of the home furniture industry, the Group has planned to increase its production capacity in a timely and cost-effective manner.

- Growth through value-accretive acquisition strategies

  To further expand its business, the Group may enter into strategic alliances, joint ventures or mergers and acquisitions with companies in the PRC.

RECENT GLOBAL FINANCIAL CRISIS

The recent global economic crisis has adversely affected the world economies and also resulted in a global credit tightening. With a deteriorating worldwide economy, demand for, among other things, consumer products may fall, which in turn may affect the demand for the Group's furniture products. If this economic downturn continues, the Group's business operations and financial performance could be adversely affected. For the first quarter of 2009, the Group's domestic sales, export sales, and licensing income decreased by approximately [15.1]%, [12.8]% and [14.6]% respectively as compared with the corresponding period of 2008.

In addition, amid the credit tightening environment, banks may vary the terms of bank loans or the banking facilities currently extended to borrowers. As at the Latest Practicable Date, the Group had banking facilities of RMB70 million, of which RMB[12] million was undrawn. Despite the increase in the lending margin imposed by the Group's lending bank effective from October 2008, the cost of funding of the Group is not expected to increase due to the reduction in the lending rate stipulated by the PBOC since September 2008.

Up to the Latest Practicable Date, the Group had not encountered any request for price cut, cancellation of orders placed, bankruptcy or default on the part of any customers and suppliers, nor had it received any notification from its principal banker regarding potential withdrawal of its banking facilities, early payment of outstanding bank borrowings, or demand for increment of collaterals for secured borrowings.

Nevertheless, the Directors observed that as a result of the slowdown of the global economy, commodities prices had generally decreased, which caused the prices of major raw materials (such as MDF board, ironware, paint and sponge) and the costs of transportation to have come down as well. During the first quarter of 2009, the average price of major raw materials and cost of transportation of the Group experienced a decrease of approximately [7.1]% and [18.9]% respectively as compared with the corresponding period of 2008. The Directors believe this would allow the Group more flexibility to adjust the product selling price, if necessary, in order to remain competitive.

The Directors believe the state of the PRC property market would have a major bearing on the growth of the Group's domestic sales and licensing business in the coming years. They are of the view that the various economic stimulus packages implemented by the PRC government will eventually restore market confidence and boost the turnover in the PRC property market, which may in turn result in an increase in the demand for furniture products. The Directors believe that the Group's domestic sales and its licensing business will benefit from the pick up in the PRC property market. Furthermore, the Group has planned to open up new markets in second and third tier cities in the PRC, such as 汕尾 (Shanwei) and 清遠 (Qingyuan) in Guangdong Province, 齊齊哈爾 (Qiqihar) in Heilongjiang Province and 福安 (Fuan) in Fujian Province to expand its distributions network in the PRC.

As for export sales, the Directors believe that countries in Africa and the Middle East, which are expected to report growth in GDP in 2009 according to the International Monetary Fund, would continue to offer new business opportunities to the Group in the coming years. The Directors also note that government authorities in the United States and Europe have announced measures aimed at supporting major institutions, stabilising markets and bolstering confidence, and a gradual recovery is projected by the International Monetary Fund in 2010. The Directors anticipate that the Group's export sales will benefit from the recovery in the global economy.

Based on the foregoing, the Directors believe that the performance of the Group in the near future may not be severely jeopardised by the current weak economic conditions. The Directors expect that the Group's future plans will continue to be implemented as scheduled. For more details, please refer to the section headed "Future plans" in this document.

RISK FACTORS

The Directors consider that the Group's business is subject to a number of risk factors which can be broadly categorised into (i) risks relating to the Group; (ii) risks relating to the industry; (iii) risks relating to the PRC; and (iv) risks relating to the Shares, details of which are set out in the section headed "Risk factors" in this document. The following is a summary of the risks referred to above:

Risks relating to the Group

- The Group is reliant on its major customers
- The licensing business is critical to the profitability of the Group
- The Group's licensing income may be subject to the manipulation of its licensees if the licensees materially understate their sales amount with their customers
- The quality of the sales services offered by the Group's distributors may be critical to the Group's brand building efforts
- The Group does not implement any measure to monitor the service quality of its overseas customers
- The Group is exposed to credit risks of its customers
- The Group's distributors may engage in price competition and market cannibalisation among themselves
- The quality of products manufactured by the licensees may not be totally subject to the Group's control
- The Group does not have any contractual relationships with the customers of its licensees, or any control over their sales operations
- The Group is dependent on its major suppliers and contract manufacturers
- The Group is reliant on its key management personnel
- There is no assurance on sustainable growth of the Group
- The Group has records of non-compliance in respect of employee social insurance and housing provident fund contributions in the PRC
- The Group has records of non-registration of lease agreements
- The Group has records of non-compliance of Hong Kong regulatory requirements
- The Group has a record of non-compliance with the Inland Revenue Ordinance
- Shenzhen Xingli and Shenzhen Xingli Zundian may be required to pay additional income tax for the Track Record Period
- The Group's newly established internal control system is not totally proven
- Any increase in the prices of raw materials or shortage of raw material supplies may adversely affect the Group's profitability
- The Group is dependent on its trademarks and other intellectual property rights
- The Group may suffer product liability claims and has limited insurance coverage

[• The Group's operation may be adversely affected by the delay in the construction of Shenzhen Xingli Zundian Production Base]

- The Group's owned properties cannot be transferred to third parties

- The Group may not be able to fulfill its obligations under an undertaking to secure its existing banking facilities
- The Group's business is subject to seasonality factors
- Implementation of the Group's future plans may not take place as planned

Risks relating to the industry

- The Group faces competition from competing brands
- Reduction in the PRC general import tariff rates may further intensify market competition
- Changes in trends of the home furniture market may affect the Group's business
- Anti-dumping duties relating to export sales could affect the Group's business
- The Group may be adversely affected by the recent global financial turmoil and economic downturn

Risks relating to the PRC

- Economic and political considerations
- Legal and regulatory considerations
- Foreign exchange rate risk

Risks relating to the Shares

- Forward-looking statements should not be unduly relied upon
- Dividends paid in the past may not be indicative of the amount of future dividend payments or the Group's future dividend policy
- The industry information and statistics contained in this document may not be unduly relied upon

TRADING RECORD

The following is a summary of the audited consolidated results of the Group for the Track Record Period. This summary is extracted from and should be read in conjunction with the accountants' report set out in Appendix I to this document.

	For the year ended 31 December		
	2006	**2007**	**2008**
	HK$'000	*HK$'000*	*HK$'000*
Turnover	369,626	492,669	534,346
Cost of sales	(299,526)	(396,438)	(433,344)
Gross profit	70,100	96,231	101,002
Other income *(Note)*	2,304	1,962	1,989
Selling and distribution expenses	(18,441)	(27,453)	(35,533)
Administrative expenses	(22,594)	(28,490)	(33,348)
Profit from operating activities	31,369	42,250	34,110
Finance costs	(481)	(18)	(70)
Profit before taxation	30,888	42,232	34,040
Taxation	(2,137)	(1,803)	(3,251)
Profit for the year	28,751	40,429	30,789
Attributable to:			
Equity holders of the Company	28,103	40,192	30,746
Minority interests	648	237	43
Profit for the year	28,751	40,429	30,789
Dividends	–	17,276	3,971

Note: Other income represents interests income, gain on disposal of equity-investment at fair value through profit or loss, dividend income, exchange gain, waiver of interest on loan from the Company's holding company and sundry income.

DIVIDEND POLICY

For the three years ended 31 December 2008, the Group declared dividends in the amount of nil, approximately HK$17.3 million and HK$[4.0] million respectively, representing dividend payout ratios of nil, approximately 42.7% and [12.9]% respectively. All of the aforesaid dividends were paid in cash out of the internal resources of the Group. The Group intends to maintain a dividend payout ratio of approximately [●]% after [●]. However, the actual dividend payout ratio will be determined at the Board's full discretion, after taking into account the profitability and cash availability of the Group. Nevertheless, the historical dividend distribution record of the Group should not be used as a reference or basis to determine the level of dividends that may be declared or paid by the Group in the future.