# FINANCIAL INFORMATION

*You should read the following discussion and analysis of our financial condition and results of operations together with our consolidated financial statements for the years ended 31 December 2006, 2007 and 2008 and the six months ended 30 June 2008 and 2009 and accompanying notes set forth in "Appendix I — Accountants' Report" to this document and other financial information appearing in this document. Our consolidated financial statements as of and for the six months ended 30 June 2008 have not been audited. Our consolidated financial statements have been prepared in accordance with IFRS.*

*The following discussion and analysis contains forward-looking statements that involve risks and uncertainties and, accordingly, you should not place undue reliance on any such statements. Our future results of operations and financial condition could differ materially from those discussed in this document. For factors that could cause or contribute to such differences, please refer to the section titled "Risk factors" and elsewhere in this document.*

## OVERVIEW

We are one of the leading PRC menswear brands. According to a market study report we commissioned from Frost & Sullivan, our LILANZ brand (which was known as LILANG prior to September 2008) ranked first in terms of retail sales for the years ended 31 December 2007 and 2008 within the mainstream PRC brands market, which comprises second and lower tier cities, and accounted for approximately 29.0% and 31.3% of the menswear market by retail sales in the PRC in 2007 and 2008, respectively. See "Industry Overview — The PRC Menswear Market" for a further discussion. In 2007 and 2008, Forbes China magazine recognised Lilang China as one of "China's Best Small & Medium-sized Enterprises". As an integrated fashion enterprise, we design, source, manufacture and sell high-quality business and casual apparel for men. We offer our customers designs for all seasons under our LILANZ brand. Our menswear products are designed for business and casual purposes and primarily target customers between the ages of 28 and 45. Our products include suits, jackets, shirts, trousers, sweaters and accessories and are broadly divided into business formal, business causal, fashion casual and sports. Our products are sold across an extensive distribution network, covering 31 provinces, autonomous regions and municipalities in the PRC.

We sell substantially all of our products on a wholesale basis to distributors who subsequently sell our products to end customers through retail outlets operated by themselves or their sub-distributors, all of whom are Independent Third Parties as of the Latest Practicable Date. Under our wholesale business model, we do not have direct contractual relationship with the sub-distributors appointed by our distributors. Along with this wholesale business model, we also operate a flagship store in Jinjiang since February 2008. All retail outlets operate under the LILANZ brand and are required to sell our products exclusively. As at 30 June 2009, 53 distributors operated or subcontracted the operation of 2,456 retail outlets.

We design our products in-house under the direction of Mr. Ji Wen Bo, one of the PRC's top fashion designers with more than 20 years of experience in the fashion industry. We manufacture a portion of our apparel at our own production facilities in Jinjiang, Fujian and outsource the rest to OEM contractors. We also outsource the production of our accessory products.

We have grown rapidly during the Track Record Period. Our turnover grew from approximately RMB418.2 million for the year ended 31 December 2006 to approximately RMB885.9 million for the year ended 31 December 2007, and to approximately RMB1,135.7 million for the year ended 31 December 2008. Our turnover grew from approximately RMB483.9 million for the six months ended 30 June 2008 to approximately RMB600.2 million for the six months ended 30 June 2009. Our profit attributable to equity shareholders increased from approximately RMB32.6 million for the year ended 31 December 2006 to RMB96.5 million for the year ended 31 December 2007, and to RMB154.1 million for the year ended 31 December 2008. Our profit attributable to equity shareholders increased from approximately RMB69.3 million for the six months ended 30 June 2008 to approximately RMB90.0 million for the six months ended 30 June 2009.

## BASIS OF PRESENTATION

Our Company was incorporated in the Cayman Islands on 2 January 2008 as an exempted company with limited liability under the Companies Law, Cap 22 (Law 3 of 1961, as consolidated and revised) of the Cayman Islands. The companies that took part in the Reorganisation, which was completed on 12 September 2008, were controlled by the same group of equity holders before and after the Reorganisation. Since there was a continuation of the risks and benefits to the controlling party, the Reorganisation is considered as a business combination under common control. The financial information of our Group for the Track Record Period as set forth in "Appendix I — Accountants' Report" has been prepared under the merger basis of accounting as if our Group had been in existence since 1 January 2006 (or where a company included in our Group was established after 1 January 2006, since the date of its establishment). The net assets of the combining companies are consolidated using the existing book values from this group of equity holders' perspective.

The consolidated income statements, the consolidated statements of comprehensive income, the consolidated statements of changes in equity and the consolidated cash flow statements of our Group for the Track Record Period as set forth in "Appendix I — Accountants' Report" include the results of operations of the companies now comprising our Group for the Track Record Period (or where the companies were established/ incorporated at a date later than 1 January 2006, for the period from the date of establishment/incorporation to 30 June 2009). The consolidated balance sheets of our Group as at 31 December 2006, 2007 and 2008 and 30 June 2009 have been prepared to present the consolidated assets and liabilities of our Group as at those dates. Intra-group balances and transactions and any unrealised profits arising from intra-group transactions are eliminated in full in preparing the consolidated financial information of our Group. Unrealised losses resulting from intra-group transactions are eliminated in the same way as unrealised gains but only to the extent that there is no evidence of impairment.

## FACTORS AFFECTING OUR RESULTS OF OPERATIONS AND FINANCIAL CONDITION

Our results of operations and financial condition have been and will continue to be affected by a number of factors, including those set out below.

### Levels of per capita disposable income and consumer spending in the PRC

We conduct all of our operations in the PRC. Economic growth in the PRC helps to drive the level of disposable income and consumer spending, which, in turn, affects the level of demand for our products. The PRC has experienced significant economic growth in recent years, achieving a CAGR for GDP of approximately 18.4% from 2001 through 2008 based on data from the NBS. According to the NBS, per capita annual disposable income of urban households, whose occupants make up the primary end customers for our products, grew from US$829 in 2001 to US$2,271 in 2008, representing a CAGR of approximately 15.5%. We believe that as disposable income has increased in the PRC, consumer spending has also increased. From 2001 through 2008, total retail sales of consumer goods grew by a CAGR of approximately 17.0%, according to data from the NBS. Furthermore, we believe that consumers in the PRC tend to be more fashion conscious and spend more on brand name products as their disposable income increases. We expect that our results of operations will continue to be significantly affected by the economic growth in the PRC. Any future slowdowns or declines in the PRC economy or consumer spending may adversely affect our business and results of operations. See "Risk Factors — Fluctuations in consumer spending caused by changes in macroeconomic conditions in the PRC may significantly affect our business, financial condition, results of operations and prospects."

### Business performance of our distributors and our ability to supervise and manage them

We sell our products to retail customers through our distributors or their sub-distributors. Our ability to increase sales is directly affected by the performance of our distributors and their sub-distributors and, in particular, the number of retail outlets that our distributors and their sub-distributors operate to sell our products.

The table below sets forth the number of our distributors and retail outlets they and their sub-distributors operated at the dates indicated and our turnover for the periods indicated.

| | As at and for the years ended 31 December | | | As at and for the six months ended 30 June | |
|---|---|---|---|---|---|
| | **2006** | **2007** | **2008** | **2008** | **2009** |
| **Number of distributors at the end of the period** | 27 | 28 | 51 | 37 | 53 |
| Number of distributors added during the period | 12 | 1 | 23 | 9 | 4 |
| Number of distributors terminated during the period | 7 | 0 | 0 | 0 | 2 |
| **Number of sub-distributors at the end of the period** | 1,338 | 1,245 | 1,257 | 1,241 | 1,185 |
| Number of sub-distributors added during the period | 422 | 183 | 156 | 82 | 47 |
| Number of sub-distributors terminated during the period | 146 | 276 | 144 | 86 | 119 |
| **Number of retail outlets at the end of the period** | 2,002 | 2,186 | 2,491 | 2,299 | 2,456 |
| Number of retail outlets added during the period | 802 | 634 | 577 | 238 | 148 |
| Number of retail outlets terminated during the period(1) | 217 | 450 | 272 | 125 | 183 |
| **Turnover** ***(RMB million)*** | 418.2 | 885.9 | 1,135.7 | 483.9(2) | 600.2 |

(1) Includes those retail outlets that were relocated to different locations within the distribution network at the discretion of the relevant distributors or sub-distributors and those smaller retail outlets that were terminated and replaced by larger retail outlets.

(2) The turnover for the six months ended 30 June 2008 is an unaudited figure.

We aim to increase the number of retail outlets to approximately 2,600 by the end of 2009. If our distributors do not continue to add new retail outlets, either by themselves or through their sub-distributors, or are otherwise unsuccessful in selling our products or we fail to effectively supervise and manage our distributors, their sub-distributors or the retail outlets they operate, our results of operations may be materially and adversely affected. See "Risk Factors — Risks Relating to Our Business — Our business may be negatively affected if our distributors or their sub-distributors fail to comply with our retail policies", "Risk Factors — Risks Relating to Our Business — We may be unable to implement and manage future rapid growth and expansion", "Business — Sales — Management of Distributors" and "Business — Sales — Management of Retail Outlets".

In addition, we rely on a small number of distributors for the sales of our products and our failure to maintain relationships with our major distributors may materially and adversely affect our results of operations. See "Risk Factors — Risks Relating to Our Business — We rely on a small number of distributors for the sales of our products and our failure to renew distributorship agreements with our major distributors or a breach of such distributorship agreements by them may materially and adversely affect our results of operations".

**Ability to maintain brand recognition**

We believe that brand recognition plays a crucial role in influencing customers' purchasing decisions. In addition, brand recognition is an important factor in our determination of the price of our products, which directly impacts our results of operations. We promote and maintain our brand name and image primarily through advertising and promotional activities and the introduction of stylish and quality designs aimed at meeting changing consumer tastes and preferences. For the years ended 31 December 2006, 2007 and 2008 and the six months ended 30 June 2008 and 2009, our advertising and promotional expenses accounted for approximately 7.3%, 9.9%, 11.2%, 10.9% and 7.3% of our turnover, respectively. We also plan to co-operate with our distributors to open flagship stores in major cities throughout the PRC, which we believe will allow us to further promote our brand by showcasing our complete line of products to customers. If we are unable to successfully maintain and promote our brand, our business and results of operations may be materially and adversely affected.

**Seasonality and weather**

Our business is affected by seasonal trends, with significantly higher levels of sales for our winter and autumn collections and lower levels of sales for our spring and summer collections. As a result, comparisons of our sales and operating results between different periods within a single year, or between different periods in different financial years, are not necessarily meaningful and cannot be relied on as indicators of our performance. See also "Risk Factors — Risks Relating to Our Business — Our business is susceptible to seasonal fluctuations and extreme or unseasonable weather conditions".

Our business is also susceptible to extreme or unseasonable weather conditions, which could have a material adverse effect on our results of operations and financial condition. For example, extended periods of unseasonably warm temperatures during the winter season or cool weather during the summer season could render a portion of our inventory incompatible with such unseasonable conditions. We are in the process of adjusting our product mix and broadening our product offerings to mitigate any adverse effects caused by unseasonable weather conditions. We cannot guarantee, however, that these efforts will be effective.

**Competition**

The menswear industry in the PRC is highly competitive with an increasing number of local and international players. We believe that we compete on the basis of brand image, design, product mix, quality, price, customer service and the breadth of our retail network. International brands traditionally dominate the high-end market, but local brands have advantages in price and sales network and are increasingly competitive in mid- to high-end markets. Our major competitors include, among others, Septwolves, Firs and Baoxiniao. We believe that the intense competition in the PRC menswear industry will continue in the future and our business and results of operations will be significantly affected by our ability to remain competitive in this industry.

**External production arrangements**

We outsource to external OEM contractors the production of our accessories, products that require special production capabilities, such as leather goods, and certain of our apparel products, especially those that we believe require less special skills and have less proprietary designs, such as certain sweaters, trousers, T-shirts and suits. All of our OEM products are manufactured under the brand name of LILANZ. Outsourced products represented approximately 34.0%, 45.7%, 42.9%, 42.9% and 63.8% of our turnover for the years ended 31 December 2006, 2007 and 2008 and the six months ended 30 June 2008 and 2009. The increase in outsourced products to 63.8% of our turnover for the six months ended 30 June 2009 primarily reflected increased sales of T-shirts and other products requiring less specialised production skill in the first half of 2009 as the distributors placed more orders for these products. We believe that our outsourcing arrangements allow us to leverage the expertise and resources of OEM contractors, and are also helpful in responding to tight schedules, especially during peak production seasons. See "Business — Production — Outsourcing" for further details on our outsourcing. However, our reliance on external OEM contractors exposes us to risks relating to the disruption of outsourced products manufactured by these contractors and if we are unable to maintain sufficient OEM production capacity, our business and results of operations may be materially and adversely affected. See "Risk Factors — Risks Relating to Our Business — We rely on our OEM contractors for the production of a significant portion of our products and any material disruption of outsourced products from our OEM contractors would materially and adversely affect our business and results of operations".

In addition, starting in 2007, we subcontracted certain production processes of a small portion of our products to other manufacturers and incurred subcontracting expenses of RMB1.6 million, RMB13.6 million, RMB3.3 million and RMB5.8 million in 2007, 2008 and the six months ended 30 June 2008 and 2009, respectively. Unlike OEM purchases, we provide raw materials to the sub-contractors for the production of these products. We believe that these sub-contracting arrangements allow us to leverage the expertise and resources of these sub-contactors and provide us with more flexibility in responding to tight schedules, while at the same time enabling us to control the quality of the raw materials used as well as certain key production processes of these products. We are still evaluating the costs and benefits of subcontracting and may use more of these arrangements going forward.

**Taxation**

Our PRC subsidiaries are subject to PRC income tax. In 2006 and 2007, the normal statutory PRC enterprise income tax rate and local income tax rate were 30% and 3%, respectively, of the assessable income as determined in accordance with the relevant PRC income tax rules and regulations. However, PRC national and local tax laws provide for various types of preferential tax treatments applicable to different enterprises.

Lilang Fujian is a foreign investment enterprise engaged in manufacturing activities in the PRC and was entitled to a preferential tax rate of 27% during 2006 and 2007. Effective 1 January 2008, the applicable tax rate for Lilang Fujian is 25% pursuant to the New Income Tax Law.

Lilang China is a foreign investment enterprise engaged in manufacturing activities in the PRC and was entitled to a preferential tax rate of 27% during 2006 and 2007. Effective 1 January 2008 and without taking into account any tax concessions, the applicable tax rate for Lilang China is 25% pursuant to the New Income Tax Law. Lilang China is also entitled to tax concessions whereby the profit for the first two financial years beginning with the first profit-making year is exempted from enterprise income tax in the PRC and the profit for each of the subsequent three years is taxed at 50% of the prevailing tax rate. Pursuant to Article 77 of the Rules for the Implementation of the Income Tax Law of the People's Republic of China for Enterprises with Foreign Investment and Foreign Enterprises (中華人民共和國外商投資企業和外國企業所得稅法實施細則), Lilang China elected to treat calendar year 2007 as the first year to enjoy the above-stated tax concessions even though it commenced operations, and recorded assessable profits, in 2006. Accordingly, Lilang China was exempted in 2007 and 2008, from PRC enterprise income tax and the applicable rate from 1 January 2009 to 31 December 2011 will be 12.5%. From 1 January 2012, the applicable tax rate for Lilang China will be 25%. The above-stated tax concessions enjoyed, or to be enjoyed, by Lilang China were approved by the Jinjiang State Tax Bureau on 16 January 2007.

Lilang Xiamen is a foreign investment enterprise engaged in manufacturing activities and established in Xiamen Special Economic Zone and is subject to PRC enterprise income tax at a rate of 18% in 2008, 20% in 2009, 22% in 2010, 24% in 2011 and 25% in 2012. Lilang Xiamen is also entitled to tax concessions whereby the profit for the first two financial years beginning from 1 January 2008 (on which the New Income Tax Law became effective) is exempted from income tax in the PRC and the profit for each of the subsequent three years is taxed at 50% of the prevailing tax rate. Accordingly, Lilang Xiamen has been exempted from PRC enterprise income tax in 2008 and will be exempted from PRC enterprise income tax in 2009. According to the current applicable laws and regulations. The applicable tax rate for Lilang Xiamen will be at 11.0% in 2010, 12.0% in 2011, 12.5% in 2012 and 25% beginning 1 January 2013.

The New Income Tax Law which became effective on 1 January 2008 revokes most preferential tax treatments for foreign-invested enterprises and adopts a unified income tax rate of 25% on most domestic enterprises and foreign-invested enterprises. Some of the existing preferential tax treatments for foreign-invested enterprises, however, will be permitted during a transition period of up to five years following the effective date of the New Income Tax Law.

Further, under the New Income Tax Law and its implementing rules, enterprises established outside the PRC with their de facto management bodies located within the PRC may be considered a PRC resident enterprise and subject to PRC enterprise income tax on their global income at the rate of 25%. Since most of our management is currently located in the PRC, we may be subject to PRC income tax at the rate of 25% on our global income. In certain circumstances, dividends received by a PRC resident enterprise from another PRC resident enterprise may be exempted from this tax, but there is no guarantee that we will qualify for this exemption.

Moreover, under the New Income Tax Law and its implementing rules, dividends payable to foreign investors that are non-resident enterprises (enterprises that do not have an establishment or place of business in the PRC, or that have such an establishment or place of business but the relevant income is not effectively connected with the establishment or place of business) are subject to a 10% withholding tax, which may be reduced if the foreign jurisdiction of incorporation has a tax treaty with the PRC that provides for a different withholding arrangement. Under grandfathering provisions, dividends declared and remitted out of the PRC from retained earnings as at 31 December 2007 are exempted from withholding tax. As such, we were liable for withholding tax on dividends distributed from our PRC subsidiaries in respect of profits generated since 1 January 2008. Pursuant to a tax arrangement between the PRC and Hong Kong, companies incorporated in Hong Kong may be subject to withholding taxes at a rate of 5% on dividends they receive from their PRC subsidiaries in which they directly hold at least 25% equity interests. As dividends from our PRC subsidiaries will be paid to us through Lilang International, our Hong Kong subsidiary, those dividends may be subject to a withholding tax at the rate of 5%.

Termination or revision of any of the preferential tax treatments that our PRC subsidiaries currently enjoy may have a material adverse effect on our results of operations.

## CRITICAL ACCOUNTING POLICIES, ESTIMATES AND JUDGMENTS

The methods, estimates and judgments the Directors use in applying our accounting policies have a significant impact on our financial position and operating results. Some of the accounting policies require us to apply estimates and judgments on matters that are inherently uncertain. The following sections discuss the accounting policies applied in preparing our financial information that we believe are most dependent on the application of these estimates and judgments, and, in addition, certain other accounting policies that we believe are material to an understanding of our financial information.

**Property, plant and equipment**

Property, plant and equipment are stated in the balance sheets at cost less accumulated depreciation and impairment losses. The cost of self-constructed items of property, plant and equipment includes cost of materials, direct labour, the initial estimate, where relevant, of the costs of dismantling and removing the items and restoring the site on which they are located, and an appropriate proportion of production overheads.

No depreciation is provided in respect of construction in progress. Upon completion and commissioning for operation, depreciation will be provided at the appropriate rates specified below. Major expenditures for improvements and renewals are recognised as separate assets. All ordinary repair and maintenance costs are expensed as incurred.

Depreciation is calculated to write off the cost of items of property, plant and equipment, less their estimated residual value, if any, using the straight-line method over their estimated useful lives as follows:

— Buildings held for our own use which are situated on leasehold land are depreciated over the shorter of the unexpired term of lease and their estimated useful lives, being no more than 40 years after the date of completion.

| | |
|---|---|
| — Plant and machinery | 10 years |
| — Motor vehicles | 5 years |
| — Furniture and fixtures | 5 years |
| — Office equipment | 5 years |
| — Leasehold improvements | Shorter of 5 years or remaining term of the lease |

We review annually the useful life of an asset and its residual value, if any, based on our historical experience with similar assets and taking into account anticipated technology changes. We will adjust depreciation expense for future periods if there are significant changes from previous estimation.

An asset's carrying amount is written down immediately to its estimated recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount.

Gains or losses arising from the retirement or disposal of an item of property, plant and equipment are determined as the difference between the net disposal proceeds and the carrying amount of the item and are recognised in income statements on the date of retirement or disposal.

**Income taxes**

Determining income tax provisions involves judgment on the future tax treatment of certain transactions and interpretation of tax rules. We have carefully evaluated tax implications of transactions and tax provisions are set up accordingly. The tax treatment of such transactions is reconsidered periodically to take into account all changes in tax legislation.

Deferred tax assets are recognised for tax losses not yet used and temporary deductible differences. As those deferred tax assets can only be recognised to the extent that it is probable that future profit will be available against which the unused tax credit can be utilised, our judgment is required to assess the probability of future taxable profits. Our assessment is constantly reviewed and additional deferred tax assets are recognised if it becomes probable that future taxable profits will allow the deferred tax asset to be recovered.

**Inventories**

Inventories are stated at the lower of cost and net realisable value. Cost is determined using the weighted average method. The cost of finished goods comprises raw materials, labour and other direct costs and related production overhead based on normal operating capacity. Net realisable value is the estimated selling price in the ordinary course of business, less applicable variable selling and distribution expenses.

We carry out physical stock counts from time to time to identify obsolete or damaged goods. We perform regular reviews of the carrying amounts of inventories with reference to aged inventories analysis, projections of expected future saleability of goods and management experience and judgment. Based on this review, write-down of inventories will be made when the carrying amounts of inventories decline below their estimated net realisable value and such policy has been consistently applied by us throughout the Track Record Period. Due to changes in market conditions, actual saleability of goods may be different from estimation and profit or loss could be affected by differences in this estimation.

**Revenue recognition**

Provided it is probable that the economic benefits will flow to us and the revenue and costs, if applicable, can be measured reliably, revenue is recognised in income statements as follows:

*Sale of goods.* We recognise revenue when the distributor has accepted the related risks and rewards of ownership (i.e., when the goods are shipped to the distributors, who pay for the transportation costs). Revenue excludes value added tax or other sales taxes and is after deduction of any trade discounts.

*Interest income.* We recognise interest income as it accures using the effective interest method.

*Government grants.* Government grants are recognised in the balance sheet initially when there is reasonable assurance that they will be received and that we will comply with the conditions attaching to them. Grants that compensate us for expenses incurred are recognised as revenue in income statements on a systematic basis during the periods in which the expenses are incurred. Grants that compensate us for the cost of an asset are deducted in arriving at the carrying amount of the asset and consequently recognised in income statements over the useful life of the asset. Unconditional discretionary government grants from the local PRC government authorities are recognised in income statements as other income on a cash receipt basis.

**Trade and other receivables**

Trade and other receivables are initially recognised at fair value and thereafter stated at amortised cost less impairment losses for bad and doubtful debts (see below), except where the receivables are interest-free loans made to related parties without any fixed repayment terms or the effect of discounting would be immaterial. In such cases, the receivables are stated at cost less impairment losses for bad and doubtful debts.

Trade and other receivables that are carried at cost or amortised cost are reviewed at each balance sheet date to determine whether there is objective evidence of impairment. Significant financial difficulties of the debtor, probability that the debtor will enter into bankruptcy or financial reorganisation, and default or delinquency in payments are considered indicators that the trade receivable is impaired. The amount of the impairment provision is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the original effective interest rate. The carrying amount of the assets is reduced through the use of an allowance account, and the amount of the loss is recognised in income statements as administrative expenses. Trade and other receivables are written off against the allowance after all means of collection have been exhausted and the potential for recovery is considered remote. Subsequent recoveries of amounts previously written off are credited against administrative expenses in income statements.

## PRINCIPAL INCOME STATEMENT COMPONENTS

### Turnover

We generate turnover primarily from the wholesale sales of our products to our distributors. Apparel generally accounts for substantially all of our turnover, representing more than 95% of our turnover for each of the years ended 31 December 2006, 2007, 2008 and the six months ended 30 June 2008 and 2009. The following table sets forth our turnover, cost of sales, gross profit, gross profit margin, number of units sold and average unit selling price for our apparel and accessories during the Track Record Period:

| | Years ended 31 December | | | | | | | | | Six months ended 30 June | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | 2006 | | | 2007 | | | 2008 | | | 2008 | | | 2009 | | |
| | Apparel | Accessories | Total | Apparel | Accessories | Total | Apparel | Accessories | Total | Apparel | Accessories | Total (Note 2) | Apparel | Accessories | Total |
| | | *RMB'000* | | | *RMB'000* | | | *RMB'000* | | | *RMB'000* | | | *RMB'000* | |
| **Turnover** | 416,139 | 2,056 | 418,195 | 872,382 | 13,539 | 885,921 | 1,096,289 | 39,395 | 1,135,684 | 476,956 | 6,989 | 483,945 | 571,008 | 29,168 | 600,176 |
| Cost of sales | (321,068) | (1,947) | (323,015) | (642,078) | (9,942) | (652,020) | (765,027) | (26,600) | (791,627) | (335,053) | (4,726) | (339,779) | (403,193) | (20,148) | (423,341) |
| **Gross profit** | 95,071 | 109 | 95,180 | 230,304 | 3,597 | 233,901 | 331,262 | 12,795 | 344,057 | 141,903 | 2,263 | 144,166 | 167,815 | 9,020 | 176,835 |
| **Gross profit margin** | 22.8% | 5.3% | 22.8% | 26.4% | 26.6% | 26.4% | 30.2% | 32.5% | 30.3% | 29.8% | 32.4% | 29.8% | 29.4% | 30.9% | 29.5% |
| **Number of units sold** | 3,462,000 | 133,000 | 3,595,000 | 7,261,000 | 286,000 | 7,547,000 | 7,718,000 | 469,000 | 8,187,000 | 3,758,000 | 96,000 | 3,854,000 | 4,458,000 | 340,000 | 4,798,000 |
| **Average unit selling price (in RMB)** *(Note 1)* | 120 | 15 | 116 | 120 | 47 | 117 | 142 | 84 | 139 | 127 | 73 | 126 | 128 | 86 | 125 |

*Note 1:* Average unit selling price is calculated by dividing the turnover for the year by the number of units sold. While this is the average unit selling price, the price per unit may vary depending on the type of apparel and accessories.

*Note 2:* The turnover, cost of sales and gross profit for the six months ended 30 June 2008 are derived from unaudited financial statements.

The following table sets forth our turnover by sales region during the Track Record Period:

| | Years ended 31 December | | | | | | Six months ended 30 June | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | 2006 | | 2007 | | 2008 | | 2008 | | 2009 | |
| | *(RMB million)* | *% of turnover* | *(RMB million)* | *% of turnover* | *(RMB million)* | *% of turnover* | *(RMB million)* | *% of turnover* | *(RMB million)* | *% of turnover* |
| **Region** | | | | | | | | | | |
| Northern PRC(1) | 26.5 | 6.3 | 81.1 | 9.1 | 80.5 | 7.1 | 36.1 | 7.5 | 40.6 | 6.8 |
| North Eastern PRC(2) | 30.7 | 7.3 | 95.5 | 10.8 | 114.2 | 10.0 | 46.9 | 9.7 | 53.9 | 9.0 |
| Eastern PRC(3) | 204.2 | 48.9 | 357.0 | 40.3 | 417.6 | 36.8 | 184.0 | 38.0 | 217.0 | 36.2 |
| Central and Southern PRC(4) | 87.8 | 21.0 | 169.7 | 19.2 | 254.9 | 22.4 | 102.1 | 21.1 | 144.9 | 24.1 |
| South Western PRC(5) | 46.7 | 11.2 | 123.9 | 14.0 | 181.2 | 16.0 | 78.0 | 16.1 | 92.2 | 15.3 |
| North Western PRC(6) | 22.3 | 5.3 | 58.7 | 6.6 | 87.3 | 7.7 | 36.8 | 7.6 | 51.6 | 8.6 |
| Total | 418.2 | 100.0 | 885.9 | 100.0 | 1,135.7 | 100.0 | 483.9 | 100.0 | 600.2 | 100.0 |

(1) Northern PRC includes Beijing, Hebei, Shanxi, Tianjin and Inner Mongolia.

(2) North Eastern PRC includes Heilongjiang, Jilin and Liaoning.

(3) Eastern PRC includes Jiangsu, Zhejiang, Shanghai, Anhui, Fujian, Shandong and Jiangxi.

(4) Central and Southern PRC includes Henan, Hubei, Hunan, Guangdong, Guangxi and Hainan.

(5) South Western PRC includes Chongqing, Sichuan, Guizhou, Yunnan and Tibet.

(6) North Western PRC includes Shaanxi, Gansu, Qinghai, Ningxia and Xinjiang.

### Cost of sales

Cost of sales consists of cost of raw materials, direct labour, sub-contracting expenses and overhead for our own production and OEM purchases. Sub-contracting expenses consist of sub-contracting charges incurred in connection with sub-contracting arrangements. Overhead costs mainly comprise indirect labour (representing primarily staff costs for our design and product development team and production and sourcing management team), fuel, electricity, depreciation of plant and machinery, rental expenses, design fees paid to external designers of our products and product development costs.

The following table sets forth our cost of sales by production cost for the Track Record Period:

| | Years ended 31 December | | | | | | | | | Six months ended 30 June | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | 2006 | | | 2007 | | | 2008 | | | 2008 | | | 2009 | | |
| Cost of Sales | *(RMB million)* | *% of cost of our own production* | *% of cost of sales* | *(RMB million)* | *% of cost of our own production* | *% of cost of sales* | *(RMB million)* | *% of cost of our own production* | *% of cost of sales* | *(RMB million)* | *% of cost of our own production* | *% of cost of sales* | *(RMB million)* | *% of cost of our own production* | *% of cost of sales* |
| *Our own production* | | | | | | | | | | | | | | | |
| Raw materials | 187.5 | 86.9 | 58.0 | 294.3 | 82.2 | 45.1 | 369.3 | 80.3 | 46.6 | 161.2 | 81.1 | 47.4 | 134.2 | 81.7 | 31.7 |
| Direct labour | 21.2 | 9.8 | 6.6 | 41.8 | 11.7 | 6.4 | 52.0 | 11.3 | 6.6 | 24.0 | 12.1 | 7.1 | 13.2 | 8.0 | 3.1 |
| Sub-contracting expenses | — | — | — | 1.6 | 0.4 | 0.3 | 13.6 | 3.0 | 1.7 | 3.3 | 1.6 | 1.0 | 5.8 | 3.5 | 1.4 |
| Overhead | 7.0 | 3.3 | 2.2 | 20.4 | 5.7 | 3.1 | 24.9 | 5.4 | 3.2 | 10.3 | 5.2 | 3.0 | 11.1 | 6.8 | 2.6 |
| Sub-total | 215.7 | 100.0 | 66.8 | 358.1 | 100.0 | 54.9 | 459.8 | 100.0 | 58.1 | 198.8 | 100.0 | 58.5 | 164.3 | 100.0 | 38.8 |
| *Outsourced production* | | | | | | | | | | | | | | | |
| OEM purchases | 107.3 | — | 33.2 | 293.9 | — | 45.1 | 331.8 | — | 41.9 | 141.0 | — | 41.5 | 259.0 | — | 61.2 |
| Total | 323.0 | — | 100.0 | 652.0 | — | 100.0 | 791.6 | — | 100.0 | 339.8 | — | 100.0 | 423.3 | — | 100.0 |

### Other revenue

Other revenue consists primarily of government grants (in the form of cash subsidies and waiver of expenses) and interest income from bank deposits.

### Selling and distribution expenses

Selling and distribution expenses consist primarily of advertising and promotional expenses which include renovation subsidies provided to our distributors, sales fair expenses and staff costs and travel expenses for our marketing and sales staff. For the years ended 31 December 2006, 2007 and 2008 and the six months ended 30 June 2008 and 2009, our selling and distribution expenses accounted for approximately 8.9%, 11.8%, 12.9%, 12.5% and 9.1%, respectively, of our turnover. Advertising and promotional expenses accounted for the vast majority of our selling and distribution expenses, representing approximately 81.8%, 83.9%, 87.0%, 87.4% and 80.1% of our selling and distribution expenses for the years ended 31 December 2006, 2007 and 2008 and the six months ended 30

June 2008 and 2009, respectively. These expenses include TV and other media advertising expenses, appointment fees for spokespersons, designing fees for new corporate logos and subsidies for renovations to retail outlets provided to distributors.

**Administrative expenses**

Administrative expenses consist primarily of staff costs for our management and administrative personnel, depreciation and amortisation, consulting fees, electricity, cost of office supplies and travel expenses. Staff costs for our management and administrative personnel represented the largest component of our administrative expenses, representing approximately 39.1%, 42.3%, 43.1%, 44.2% and 36.2% of our administrative expenses for the years ended 31 December 2006, 2007 and 2008 and the six months ended 30 June 2008 and 2009.

**Other operating (expenses)/income**

Other operating expenses for the six months ended 30 June 2009 were RMB0.2 million, which mainly represented charitable donations of RMB0.1 million and loss on disposal of fixed assets of RMB0.1 million. Other operating income for the six months ended 30 June 2008 was RMB2.2 million, mainly consisting of a gain on disposal of fixed assets of RMB3.1 million, partially offset by the charitable donations of RMB0.5 million. Other operating income for the year ended 31 December 2008 was RMB1.9 million, primarily as a result of a gain of RMB3.1 million in connection with the disposal of our headquarter premises in Jinjiang, Fujian in February 2008 which was partially offset by charitable donations of RMB0.8 million. Other operating expenses for 2007 were RMB1.8 million, consisting of charity donations of RMB0.7 million, losses of RMB0.5 million incurred on disposal of certain fixed assets and write-off of RMB0.6 million of design fees for certain product designs which were not adopted. Other operating expenses for 2006 were RMB0.6 million, consisting of a one-time compensation payment made to a distributor who alleged a breach of sales contract against us in 2006.

**Finance costs**

Finance costs consist primarily of interest on bank borrowings wholly repayable within one year.

**Income tax**

Income tax represents amounts of PRC enterprise income tax paid by our Group. Our Group was not subject to Hong Kong profits tax or any income tax in the Cayman Islands or the BVI during the Track Record Period. Our Group's effective income tax rate, calculated as our Group's income tax expense divided by profit before taxation, was approximately 28.6%, 1.3%, 3.4%, 2.9% and 13.3% in 2006, 2007 and 2008 and the six months ended 30 June 2008 and 2009, respectively. Our effective income tax rate decreased from approximately 28.6% in 2006 to approximately 1.3% in 2007, primarily because Lilang China, through which we conducted the vast majority of our business in 2007, elected to treat 2007 as the first profit-making year for PRC enterprise income tax purposes and therefore was exempted from PRC enterprise income tax in that year. Our effective income tax rate increased slightly from approximately 1.3% in 2007 to approximately 3.4% 2008, primarily because deferred tax liabilities were recognised in 2008 in respect of the undistributed profits earned by our subsidiaries in the PRC since 1 January 2008 and a PRC land appreciation tax incurred on the disposal of our headquarter premises in Jinjiang, Fujian in February 2008. Our effective income tax rate increased from approximately 2.9% for the six months ended 30 June 2008 to 13.3% for the six months ended 30 June 2009, primarily because Lilang China was subject to the PRC enterprise income tax at 12.5% since 1 January 2009. Lilang China was exempted from the PRC enterprise income tax in 2008.

The applicable PRC enterprise income tax rates during the Track Record Period for our PRC subsidiaries, Lilang China, Lilang Fujian and Lilang Xiamen, through which we conduct all of our operations, are set out below:

| | Years ended 31 December | | | Six months ended 30 June |
|---|---|---|---|---|
| | **2006** | **2007** | **2008** | **2009** |
| Lilang China | 27% | Tax exemption(1) | Tax exemption(1) | 12.5%(1) |
| Lilang Fujian | 27% | 27% | 25% | 25% |
| Lilang Xiamen | N/A | N/A | Tax exemption | Tax exemption |

(1) Lilang China elected to treat 2007 as the first profit-making year for PRC enterprise income tax purposes and therefore was exempted from PRC enterprise income tax in 2007 and 2008 and is subject to a reduced rate of 12.5% in 2009, 2010 and 2011.

See "Factors Affecting Our Results of Operations and Financial Condition — Taxation" in this section of the document for more information on the applicable PRC enterprise income tax rates for our PRC subsidiaries.

## RESULTS OF OPERATIONS

The following table sets forth the summary consolidated income statement data of our Group for the Track Record Period. We have derived the summary consolidated income statement data of our Group from our consolidated financial statements which have been prepared in accordance with IFRS, set forth in the section headed " Appendix I — Accountants' Report".

| | Years ended 31 December | | | Six months ended 30 June | |
|---|---|---|---|---|---|
| | **2006** | **2007** | **2008** | **2008** | **2009** |
| | *(RMB million, except per share data)* | | | *(unaudited)* | |
| **Turnover** | 418.2 | 885.9 | 1,135.7 | 483.9 | 600.2 |
| Cost of sales | (323.0) | (652.0) | (791.6) | (339.8) | (423.3) |
| **Gross profit** | 95.2 | 233.9 | 344.1 | 144.1 | 176.9 |
| Other revenue | 1.5 | 5.2 | 5.8 | 5.3 | 1.2 |
| Selling and distribution expenses | (37.3) | (104.9) | (146.5) | (60.3) | (54.6) |
| Administrative expenses | (9.2) | (22.7) | (34.3) | (15.4) | (15.2) |
| Other operating (expenses)/ income | (0.7) | (1.8) | 1.9 | 2.2 | (0.2) |
| **Profit from operations** | 49.5 | 109.7 | 171.0 | 75.9 | 108.1 |
| Finance costs | (3.9) | (12.0) | (11.5) | (4.6) | (4.3) |
| **Profit before taxation** | 45.6 | 97.7 | 159.5 | 71.3 | 103.8 |
| Income tax | (13.0) | (1.2) | (5.4) | (2.0) | (13.8) |
| **Profit attributable to equity shareholders** | 32.6 | 96.5 | 154.1 | 69.3 | 90.0 |
| **Basic earnings per share (RMB (cents))** | 3.62 | 10.72 | 17.13 | 7.70 | 10.00 |

The following table sets forth the summary consolidated income statement data of our Group as a percentage of consolidated turnover for the Track Record Period.

| | Years ended 31 December | | | Six months ended 30 June | |
|---|---|---|---|---|---|
| | 2006 | 2007 | 2008 | 2008 | 2009 |
| | *(% of turnover)* | | | | |
| | | | | *(unaudited)* | |
| Turnover | 100.0% | 100.0% | 100.0% | 100.0% | 100.0% |
| Cost of sales | (77.2%) | (73.6%) | (69.7%) | (70.2%) | (70.5%) |
| **Gross profit** | 22.8% | 26.4% | 30.3% | 29.8% | 29.5% |
| Other revenue | 0.3% | 0.6% | 0.5% | 1.1% | 0.2% |
| Selling and distribution expenses | (8.9%) | (11.8%) | (12.9%) | (12.5%) | (9.1%) |
| Administrative expenses | (2.2%) | (2.6%) | (3.0%) | (3.2%) | (2.5%) |
| Other operating (expenses)/ income | (0.2%) | (0.2%) | 0.2% | 0.5% | (0.03%) |
| **Profit from operations** | 11.8% | 12.4% | 15.1% | 15.7% | 18.0% |
| Finance costs | (0.9%) | (1.4%) | (1.0%) | (1.0%) | (0.7%) |
| **Profit before taxation** | 10.9% | 11.0% | 14.1% | 14.7% | 17.3% |
| Income tax | (3.1%) | (0.1%) | (0.5%) | (0.4%) | (2.3%) |
| **Profit attributable to equity shareholders** | 7.8% | 10.9% | 13.6% | 14.3% | 15.0% |

**Six months ended 30 June 2009 compared to six months ended 30 June 2008 (unaudited)**

*Turnover*. Turnover increased by approximately 24.0% from RMB483.9 million for the six months ended 30 June 2008 to RMB600.2 million for the six months ended 30 June 2009, primarily due to increased sales volume. The number of units we sold increased from 3,854,000 units for the six months ended 30 June 2008 to 4,798,000 units for the six months ended 30 June 2009, primarily attributable to growing recognition of our LILANZ brand, the expansion of our product offerings and the continued expansion of our distribution network. As at 30 June 2009, the number of the retail outlets operated by our distributors and their sub-distributors was 2,456, compared to 2,299 as at 30 June 2008. The overall average unit selling price of our products remained relatively stable at RMB125 for the six months ended 30 June 2009 when compared to RMB126 for the six months ended 30 June 2008. The average unit selling price of our apparel products increased from RMB127 for the six months ended 30 June 2008 to RMB128 for the six months ended 30 June 2009. The average unit selling price of our accessories products increased from RMB73 for the six months ended 30 June 2008 to RMB86 for the six months ended 30 June 2009.

Turnover increased in all of our sales regions for the six months ended 30 June 2009 compared to the six months ended 30 June 2008: turnover generated in the North Eastern PRC region increased by approximately 14.9% from RMB46.9 million for the six months ended 30 June 2008 to RMB53.9 million for the six months ended 30 June 2009; turnover generated in the Eastern PRC region increased by approximately 17.9% from RMB184.0 million for the six months ended 30 June 2008 to RMB217.0 million for the six months ended 30 June 2009; turnover generated in the Central and Southern PRC region increased by approximately 41.9% from RMB102.1 million for the six months ended 30 June 2008 to RMB144.9 million for the six months ended 30 June 2009; turnover generated in the South Western PRC region increased by approximately 18.2% from RMB78.0 million for the six months ended 30 June 2008 to RMB92.2 million for the six months ended 30 June 2009; and turnover generated in the North Western PRC region increased by approximately 40.2% from RMB36.8 million for the six months ended 30 June 2008 to RMB51.6 million for the six months ended 30 June 2009. The Eastern PRC region remained as our top sales region, accounting for approximately 36.2% of our turnover for the six months ended 30 June 2009.

*Cost of sales.* Cost of sales increased by approximately 24.6% from RMB339.8 million for the six months ended 30 June 2008 to RMB423.3 million for the six months ended 30 June 2009, driven by an increase in cost of outsourced production, largely due to an increase in sales of outsourced products. Cost of our own production decreased by approximately 17.4% from RMB198.8 million for the six months ended 30 June 2008 to RMB164.3 million for the six months ended 30 June 2009. Cost of raw materials as a percentage of total cost of our own production increased slightly from approximately 81.1% for the six months ended 30 June 2008 to 81.7% for the six months ended 30 June 2009. Overhead cost as a percentage of total cost of our own production increase from approximately 5.2% for the six months ended 30 June 2008 to approximately 6.8% for the six months ended 30 June 2009, primarily due to the increase in our rental expenses for our factory in Meiling and research centre in Shanghai which we leased in March 2008 and October 2008, respectively. Sub-contracting expenses as a percentage of total cost of our own production increased from approximately 1.6% to approximately 3.5% for the six months ended 30 June 2009, primarily due to the increase in subcontracting activities in 2009.

Cost of outsourced production increased by approximately 83.7% from RMB141.0 million for the six months ended 30 June 2008 to RMB259.0 million for the six months ended 30 June 2009. Cost of outsourced production as a percentage of total cost of sales increase from approximately 41.5% for the six months ended 30 June 2008 to approximately 61.2% for the six months ended 30 June 2009, primarily as a result of the increase in the sales of outsourced products compared to self-produced products.

*Gross profit and gross profit margin.* Gross profit increased by approximately 22.7% from RMB144.1 million for the six months ended 30 June 2008 to RMB176.9 million for the six months ended 30 June 2009, primarily as a result of an increase in the turnover. Our gross profit margin remained relatively stable at 29.5% for the six months ended 30 June 2009, compared to 29.8% for the six months ended 30 June 2008. The slight decrease in profit margin was primarily due to the fact that we sold a larger portion of lower-margin outsourced products for the first half of 2009, which was largely offset by increased economies of scale in our purchasing power as a result of increased sales volume.

*Other revenue*. Other revenue decreased from RMB5.3 million for the six months ended 30 June 2008 to RMB1.2 million for the six months ended 30 June 2009, primarily as a result of a decrease in interest income from deposits and a decrease in government grants.

*Selling and distribution expenses*. Selling and distribution expenses decreased by approximately 9.5% from RMB60.3 million for the six months ended 30 June 2008 to RMB54.6 million for the six months ended 30 June 2009, primarily due to a decrease in advertising and promotional expenses by RMB9.0 million which was partially offset by an increase in expenses incurred for sales fairs and staff costs.

*Administrative expenses*. Administrative expenses decreased by 1.4% from RMB15.4 million for the six months ended 30 June 2008 to RMB15.2 million for the six months ended 30 June 2009. We anticipate a significant increase in administrative expenses going forward in connection with the needs of a listed company, including fees of professional advisors and accountants for ongoing reporting obligations and regulatory compliance.

*Other operating expenses/income*. We recorded other operating income of RMB2.2 million for the six months ended 30 June 2008 primarily as a result of gain on disposal of fixed assets. We recorded other operating expenses of RMB0.2 million for the six months ended 30 June 2009, consisting primarily of charitable donations and loss on disposal of fixed assets.

*Finance costs*. Finance costs decreased by approximately 6.1% from RMB4.6 million for the six months ended 30 June 2008 to RMB4.3 million for the six months ended 30 June 2009, primarily as a result of a decrease in interest rates.

*Profit before taxation*. As a result of the foregoing factors, profit before taxation increased by approximately 45.4% from RMB71.3 million for the six months ended 30 June 2008 to RMB103.8 million for the six months ended 30 June 2009.

*Income tax*. Income tax expense increased from RMB2.0 million for the six months ended 30 June 2008 to RMB13.8 million for the six months ended 30 June 2009 and our effective income tax rate increased from approximately 2.9% for the six months ended 30 June 2008 to approximately 13.3% for the six months ended 30 June 2009, in each case, primarily because for the six months ended 30 June 2009, Lilang China was subject to PRC enterprise income tax at a rate of 12.5% in 2009 while it was exempt from the PRC enterprise income tax in 2008.

*Profit attributable to equity shareholders*. As a result of the foregoing factors, profit attributable to equity shareholders increased by approximately 29.8% from RMB69.3 million for the six months ended 30 June 2008 to RMB90.0 million for the six months ended 30 June 2009. Our net profit margin increased to approximately 15.0% for the six months ended 30 June 2009 from approximately 14.3% for the six months ended 30 June 2008.

**2008 compared to 2007**

*Turnover*. Turnover increased by approximately 28.2% from RMB885.9 million in 2007 to RMB1,135.7 million in 2008, primarily due to increases in both the average selling price and sales volume. The average unit selling price of our products increased from RMB117 in 2007 to RMB139 in 2008. This increase was attributable to a shift in product mix towards higher priced apparel and accessories. The number of units we sold also increased from 7,547,000 units in 2007 to 8,187,000 units in 2008. Such increases were the result of the growing recognition of our LILANZ brand, the expansion of our product offerings and the continued expansion of our distribution network. As at 31 December 2008, the number of the retail outlets operated by our distributors and their sub-distributors was 2,491, compared to 2,186 as at 31 December 2007.

Turnover increased in five of our sales regions in 2008 compared to 2007: turnover generated in the North Eastern PRC region increased by approximately 19.6% from RMB95.5 million in 2007 to RMB114.2 million in 2008; turnover generated in the Eastern PRC region increased by approximately 17.0% from RMB357.0 million in 2007 to RMB417.6 million in 2008; turnover generated in the Central and Southern PRC region increased by approximately 50.2% from RMB169.7 million in 2007 to RMB254.9 million in 2008; turnover generated in the South Western PRC region increased by approximately 46.2% from RMB123.9 million in 2007 to RMB181.2 million in 2008; and turnover generated in the North Western PRC region increased by approximately 48.7% from RMB58.7 million in 2007 to RMB87.3 million in 2008. Our turnover in the Northern PRC region decreased slightly from RMB81.1 million in 2007 to RMB80.5 million in 2008. The Eastern PRC region remained as our top sales region, accounting for approximately 36.8% of our turnover in 2008.

*Cost of sales*. Cost of sales increased by approximately 21.4% from RMB652.0 million in 2007 to RMB791.6 million in 2008, driven by an increase in both cost of our own production and cost of outsourced production, largely consistent with an increase in our sales volume. Cost of our own production increased by approximately 28.4% from RMB358.1 million for 2007 to RMB459.8 million for 2008. Cost of raw materials as a percentage of total cost of our own production decreased from approximately 82.2% in 2007 to 80.3% in 2008. Overhead cost as a percentage of total cost of our own production decreased from approximately 5.7% in 2007 to approximately 5.4% in 2008, primarily due to the decrease in our rental expenses for our factory in 2008 as we leased less space for our warehouse and production in 2008 as compared to 2007 as construction of Wuli Industrial Park was completed in 2008. Sub-contracting expenses as a percentage of total cost of our own production increased from approximately 0.4% to approximately 3.0% in 2008. We started to sub-contract certain production processes to third party contractors on a trial basis in 2007. We sub-contracted these production processes to the third party contractors on a larger scale in 2008.

Cost of outsourced production increased by approximately 12.9% from RMB293.9 million in 2007 to RMB331.8 million in 2008. Cost of outsourced production as a percentage of total cost of sales decreased from approximately 45.1% in 2007 to approximately 41.9% in 2008, primarily as a result of the decrease in the sales of outsourced products compared to self-produced products.

*Gross profit and gross profit margin.* Gross profit increased by approximately 47.1% from RMB233.9 million in 2007 to RMB344.1 million in 2008, primarily as a result of an increase in the turnover. Our gross profit margin increased to approximately 30.3% in 2008 from approximately 26.4% in 2007, primarily as a result of increased sales of higher margin products and greater economies of scale in our purchasing power as a result of increased sales volume in 2008.

*Other revenue.* Other revenue increased from RMB5.2 million in 2007 to RMB5.8 million in 2008, primarily as a result of higher government grants.

*Selling and distribution expenses.* Selling and distribution expenses increased by approximately 39.6% from RMB104.9 million in 2007 to RMB146.5 million in 2008, primarily due to the increased renovation subsidies of RMB32.2 million incurred for the refurbishment of the retail outlets of our distributors in 2008.

*Administrative expenses.* Administrative expenses increased by approximately 51.2% from RMB22.7 million in 2007 to RMB34.3 million in 2008, primarily due to (i) an increase in staff costs for our management and administrative personnel, which increased from RMB9.6 million in 2007 to RMB14.8 million in 2008, driven by higher average employee salary which was partially offset by a decrease in headcount in 2008 and (ii) an increase in cost of office supplies and travel expenses, which increased from RMB3.5 million to RMB5.2 million, as a result of the general expansion of our business.

*Other operating expenses/income.* We recorded other operating income in 2008 of RMB1.9 million primarily as a result of a gain of RMB3.1 million in connection with the disposal of our headquarter premises in Jinjiang, Fujian in February 2008 which was partially offset by our charitable donations of RMB0.8 million. We recorded other operating expenses of RMB1.8 million in 2007, consisting primarily of charitable donations of RMB0.7 million, loss of RMB0.5 million incurred on disposal of certain fixed assets and write-off of RMB0.6 million of design fees for certain product designs which were not adopted.

*Finance costs.* Finance costs decreased by approximately 3.7% from RMB12.0 million in 2007 to RMB11.5 million in 2008, primarily as a result of a decrease in interest rates on our bank borrowings in the first half of the year in 2008.

*Profit before taxation.* As a result of the foregoing factors, profit before taxation increased by approximately 63.2% from RMB97.7 million in 2007 to RMB159.5 million in 2008.

*Income tax.* Income tax expense increased by approximately 337.6% from RMB1.2 million in 2007 to RMB5.4 million in 2008 and our effective income tax rate increased from approximately 1.3% in 2007 to approximately 3.4% in 2008, in each case, primarily because of the increase in profit before taxation in 2008 and the fact that deferred tax liabilities were recognised in 2008 in respect of the undistributed profits earned by the subsidiaries of our Company in the PRC since 1 January 2008 and a PRC land appreciation tax incurred on the disposal of our headquarter premises in Jinjiang, Fujian Province in February 2008.

*Profit attributable to equity shareholders.* As a result of the foregoing factors, profit attributable to equity shareholders increased by approximately 59.7% from RMB96.5 million in 2007 to RMB154.1 million in 2008. Our net profit margin increased to approximately 13.6% in 2008 from approximately 10.9% in 2007.

**2007 compared to 2006**

*Turnover.* Turnover increased by approximately 111.8% from RMB418.2 million in 2006 to RMB885.9 million in 2007, primarily due to increased sales volume. The number of units sold increased from 3,595,000 units in 2006 to 7,547,000 units in 2007. Such increase was due to an expansion of distribution network and broader product offerings and stronger overall demand for our products due to the strengthening of our brand image. As at 31 December 2007, the number of the retail outlets operated by our distributors and their sub-distributors reached 2,186, compared to 2,002 as at 31 December 2006. The expansion of our product offerings was primarily due to the strengthening of our product design and development capability as Mr. Ji Wen Bo joined us full time as our chief designer in 2007. The overall average unit selling price of our products was relatively stable at RMB116 in 2006 as compared to RMB117 in 2007.

Turnover increased in all of our six sales regions in 2007 compared to 2006: turnover generated in the Northern PRC region increased by approximately 206.0% from RMB26.5 million in 2006 to RMB81.1 million in 2007; turnover generated in the North Eastern PRC region increased by approximately 211.1% from RMB30.7 million in 2006 to RMB95.5 million in 2007; turnover generated in the Eastern PRC region increased by approximately 74.8% from RMB204.2 million in 2006 to RMB357.0 million in 2007; turnover generated in the Central and Southern PRC region increased by approximately 93.3% from RMB87.8 million in 2006 to RMB169.7 million in 2007; turnover generated in the South Western PRC region increased by approximately 165.3% from RMB46.7 million in 2006 to RMB123.9 million in 2007; and turnover generated in the North Western PRC region increased by approximately 163.2% from RMB22.3 million in 2006 to RMB58.7 million in 2007. The Eastern PRC region remained as our top sales region, accounting for approximately 40.3% of our turnover in 2007.

*Cost of sales.* Cost of sales increased by approximately 101.9% from RMB323.0 million in 2006 to RMB652.0 million in 2007, driven by an increase in both cost of our own production and cost of outsourced production, which, in turn, was driven by a higher sales volume. Cost of our own production increased by approximately 66.0% from RMB215.7 million for 2006 to RMB358.1 million for 2007. Cost of raw materials as a percentage of total cost of our own production decreased from approximately 86.9% in 2006 to approximately 82.2% in 2007, primarily due to the fact that we incurred proportionally more cost of direct labour and overhead cost in 2007. Cost of direct labour as a percentage of total cost of our own production increased from approximately 9.8% in 2006 to approximately 11.7% in 2007, primarily because of the increase in our provision for retirement benefit contributions in respect of our direct labour from RMB1.7 million in 2006 to RMB6.5 million in 2007 and the fact that in 2007, as compared to 2006, we produced proportionally more products requiring special skills or with special designs in house, which were generally more labour-intensive. Overhead cost as a percentage of total cost of our own production increased from approximately 3.3% in 2006 to approximately 5.7% in 2007, primarily due to an increase in cost of indirect labour, driven by higher employee headcount in our design and production team and sourcing management team.

Cost of outsourced production increased by approximately 173.9% from RMB107.3 million in 2006 to RMB293.9 million in 2007. Cost of outsourced production as a percentage of total cost of sales increased from approximately 33.2% in 2006 to approximately 45.1% in 2007, primarily as a result of increase in the sales of outsourced products compared to self-produced products.

*Gross profit and gross profit margin.* Gross profit increased by approximately 145.7% from RMB95.2 million in 2006 to RMB233.9 million in 2007, primarily as a result of an increase in the turnover. Our gross profit margin increased to approximately 26.4% in 2007 from approximately 22.8% in 2006, primarily as a result of greater economies of scale in our purchasing power as a result of increased sales volume in 2007.

*Other revenue.* Other revenue increased from RMB1.5 million in 2006 to RMB5.2 million in 2007, primarily as a result of the higher interest income and government grants.

*Selling and distribution expenses.* Selling and distribution expenses increased by approximately 180.9% from RMB37.3 million in 2006 to RMB104.9 million in 2007, primarily due to an increase of approximately 188.5% in advertising and promotional expenses from RMB30.5 million to RMB88.0 million.

*Administrative expenses.* Administrative expenses increased by approximately 145.7% from RMB9.2 million in 2006 to RMB22.7 million in 2007, primarily due to (i) an increase in staff costs for our management and administrative personnel, which increased from RMB3.6 million in 2006 to RMB9.6 million in 2007, driven by higher employee head count and average employee salary, (ii) an increase in cost of office supplies and travel expenses, which increased from RMB1.1 million to RMB3.5 million, as a result of the general expansion of our business, and (iii) consultancy fees of RMB1.5 million paid in 2007 in respect of certain financial advice obtained by our Group in connection with a proposed reorganisation and [●] of our Group.

*Other operating expenses.* Other operating expenses increased from RMB0.7 million in 2006 to RMB1.8 million in 2007, consisting primarily of charity donations of RMB0.7 million, a loss of RMB0.5 million incurred on disposal of certain fixed assets and a write-off of RMB0.6 million of design fees for certain product designs which were not adopted.

*Finance costs.* Finance costs increased by approximately 207.3% from RMB3.9 million in 2006 to RMB12.0 million in 2007, primarily as a result of an increase in our bank borrowings.

*Profit before taxation.* As a result of the foregoing factors, profit before taxation increased by approximately 114.3% from RMB45.6 million in 2006 to RMB97.7 million in 2007.

*Income tax.* Income tax expense decreased by approximately 90.6% from RMB13.0 million in 2006 to RMB1.2 million in 2007 and our effective income tax rate decreased from approximately 28.6% in 2006 to approximately 1.3% in 2007, in each case, primarily because Lilang China, through which we conducted the vast majority of our business in 2007, elected to treat 2007 as the first profit-making year for PRC enterprise income tax purposes and therefore was exempted from PRC enterprise income tax in that year.

*Profit attributable to equity shareholders.* As a result of the foregoing factors, profit attributable to equity shareholders increased by approximately 196.2% from RMB32.6 million in 2006 to RMB96.5 million in 2007. Our net profit margin increased to approximately 10.9% in 2007 from approximately 7.8% in 2006.

## LIQUIDITY AND CAPITAL RESOURCES

Our primary uses of cash are to fund our working capital requirements, including trade payables and product development, manufacturing and operating expenses, fund capital expenditures related to the construction of new production and other facilities and repay loans and related interest. We have historically funded our cash requirements primarily from cash flow generated from operations, proceeds from a controlling shareholder and bank loans. There have been no material changes in our underlying drivers of the sources and uses of cash during the Track Record Period.

Going forward, we intend to satisfy our liquidity requirements using a combination of the proceeds from the [●], cash flow generated from operations, bank loans and future debt and securities offerings. However, our ability to fund our future liquidity requirements are subject to prevailing economic conditions, the availability of debt financing and other factors, many of which are beyond our control. See "Risk factors — Risks Relating to Our Business — Our ability to obtain additional financing may be limited, which could delay or prevent the completion of one or more of our strategies."

The following table presents selected cash flow data from our Group's consolidated cash flow statements for the Track Record Period, as derived from "Appendix I — Accountants' Report".

| | Years ended 31 December | | | Six months ended 30 June | |
|---|---|---|---|---|---|
| | 2006 | 2007 | 2008 | 2008 | 2009 |
| | | | | *(unaudited)* | |
| | *(RMB million)* | | | | |
| Net cash (used in)/generated from operating activities | (109.3) | 91.9 | 43.1 | (14.1) | 106.4 |
| Net cash used in investing activities | (61.5) | (16.5) | (92.2) | (43.0) | (11.6) |
| Net cash generated from/ (used in) financing activities | 187.4 | (44.2) | 44.1 | 28.1 | (54.1) |
| Net increase/(decrease) in cash | 16.6 | 31.2 | (5.0) | (29.0) | 40.7 |
| Cash at the beginning of the year/period | 10.6 | 27.3 | 58.5 | 58.5 | 53.6 |
| Cash at the end of the year/ period | 27.2 | 58.5 | 53.5 | 29.5 | 94.3 |

**Operating activities**

For the six months ended 30 June 2009, we had net cash generated from operating activities of RMB106.4 million which was primarily contributed by cash generated from operating profit before changes in working capital of RMB113.2 million and a decrease in other receivables of RMB95.8 million. These cash inflows were partially offset by an increase in inventories of RMB14.5 million, an increase in trade and bills receivables of RMB53.8 million and a decrease in trade and bills payables of RMB42.2 million. The increase in trade and bills receivables was primarily due to the increase in our sales.

For the six months ended 30 June 2008, net cash used in operating activities amounted to RMB14.1 million which was primarily contributed by an increase in trade and bills receivables of RMB74.6 million and decrease in trade and bills payables of RMB45.6 million. These cash outflows were partially offset by the cash generated from operations before changes in working capital of RMB75.2 million and a decrease in other receivables of RMB41.1 million.

In 2008, we had net cash generated from operating activities of RMB43.1 million, which was primarily contributed by an operating profit before changes in working capital of RMB173.0 million. These cash inflows were partially offset by an increase in inventories of RMB75.5 million, an increase in trade and bills receivables of RMB79.4 million and a decrease in trade and bills payables of RMB38.5 million. The increase in trade and bills receivables was primarily due to the increase in our sales.

In 2007, we had net cash generated from operating activities of RMB91.9 million, which was primarily contributed by an operating profit before changes in working capital of RMB111.0 million and an increase in trade and bills payables of RMB167.5 million. These cash inflows were partially offset by an increase in trade receivables of RMB17.8 million, an increase in other receivables of RMB76.1 million, an increase in inventories of RMB55.7 million and an increase in pledged bank deposits of RMB39.0 million. The increase in trade and bills payable was primarily due to an increase in our purchase of raw materials and OEM products as a result of the increase in demand for our products; the increase in other receivables was primarily due to the increase in prepayments to suppliers and our prepaid advertising expenses and prepayment for store displays to be provided to our distributors as renovation subsidies; and the increase in inventories was primarily attributable to increases in our sales and the fact that the sales fair for the spring and summer collections in 2007 was held in October 2006, while the sales fair for the spring and summer collections in 2008 was held in September 2007, which resulted in an increase in completed products and higher inventory level as at 31 December 2007.

In 2006, we had net cash used in operating activities of RMB109.3 million, which was primarily contributed by an increase in trade receivables of RMB142.6 million, an increase in other receivables of RMB36.3 million and an increase in inventories of RMB23.3 million. These cash outflows were partially offset by an operating profit before changes in working capital of RMB51.1 million and an increase in trade and bills payables of RMB41.3 million. The increase in trade receivables was primarily due to the increase in our turnover and extended credit terms granted by us to select creditworthy distributors in 2006 to expand their retail network for our products, in line with our growth objective; the increase in other receivables was primarily due to the increase in prepayments to suppliers; the increase in inventories was primarily attributable to increases in our sales; and the increase in trade and bills payable was primarily due to an increase in our purchase of raw materials and OEM products as a result of the increase in demand for our products.

**Investing activities**

For the six months ended 30 June 2009, net cash used in investing activities amounted to RMB11.6 million, primarily for payments for the purchase of property, plant and equipment in connection with the construction of our production facilities in Wuli Industrial Park in the aggregate amount of RMB11.8 million.

For the six months ended 30 June 2008, net cash used in investing activities amounted to RMB43.0 million, primarily for payments for the purchase of property, plant and equipment in connection with the construction of our production facilities in Wuli Industrial Park in the aggregate amount of RMB40.7 million.

In 2008, net cash used in investing activities amounted to RMB92.2 million, primarily for payments for the purchase of property, plant and equipment in connection with the construction of our production facilities in Wuli Industrial Park in the aggregate amount of RMB60.3 million and payment for the purchase of investment property in the aggregate amount of RMB30.1 million in connection with the premises in Zhengzhou.

In 2007, net cash used in investing activities amounted to RMB16.5 million, primarily for payments for the purchase of property, plant and equipment in connection with the construction of our production facilities in the Wuli Industrial Park in the aggregate amount of RMB60.4 million and a loan to Fujian Strait West Coast Investment Co., Ltd. (福建海峽西岸投資有限公司), or Fujian Strait, a real estate developer and an Independent Third Party, in the amount of RMB30.0 million. These cash outflows were partially offset by repayments of amounts due from Jinjiang Xiaosheng Apparel Enterprise Limited (晉江曉升服裝實業有限公司), or Jinjiang Xiaosheng, and Jinjiang Menglang Apparel Limited (晉江市猛郎服飾有限公司), or Jinjiang Menglang, each, a related party, in the aggregate amount of RMB42.5 million and repayments of the loan to Fujian Strait in the aggregate amount of RMB30.0 million. The loan to Fujian Strait was made in March 2007 and due in December 2007. The principal and accrued interest of the loan were subsequently repaid in full.

In 2006, net cash used in investing activities amounted to RMB61.5 million, primarily for payment of advances to Jinjiang Xiaosheng and Jinjiang Menglang in the aggregate amount of RMB25.2 million, payments for the construction of our production facilities in the Wuli Industrial Park in the aggregate amount of RMB12.7 million and prepayments for the purchase of land use rights for our production facilities in the Wuli Industrial Park and our planned research and product development facilities in Xiamen, Fujian in the aggregate amount of RMB16.3 million.

**Financing activities**

For the six months ended 30 June 2009, we had net cash used in financing activities of RMB54.1 million, which was primarily the result of repayments of bank loans in the aggregate amount of RMB212.0 million, partially offset by the proceeds from bank loans for working capital purposes in the aggregate amount of RMB170.0 million.

For the six months ended 30 June 2008, we had net cash generated from financing activities of RMB28.1 million, which was primarily contributed by proceeds from bank loans in the aggregate amount of RMB160.0 million and advances from our Controlling Shareholders of RMB16.2 million, partially offset by repayment of bank loans of RMB124.5 million and payments of expenses relating to our proposed [●] of RMB19.4 million.

In 2008, we had net cash generated from financing activities of RMB44.1 million, which was primarily contributed by proceeds from bank loans for working capital purposes in the aggregate amount of RMB300.0 million and advances from a shareholder in the aggregate amount of RMB29.4 million, partially offset by repayment of bank loans in the aggregate amount of RMB254.5 million and payment of expenses relating to the proposed offering.

In 2007, net cash used in financing activities amounted to RMB44.2 million, which was primarily the result of repayments of bank loans in the aggregate amount of RMB445.5 million and payments of interest of RMB11.6 million, partially offset by the proceeds from bank loans for working capital purposes in the aggregate amount of RMB414.5 million.

In 2006, we had net cash generated from financing activities of RMB187.4 million, which was primarily contributed by proceeds from bank loans of RMB135.5 million for working capital purposes and proceeds from a shareholder loan of RMB108.2 million, partially offset by the repayments of bank loans in the amount of RMB54.1 million.

**Inter-enterprise financing activities**

In addition to the loan granted by Lilang Fujian to Fujian Strait in the amount of RMB30.0 million which accrued interest in the amount of RMB2.15 million in 2007, we granted certain cash advances in an aggregate amount of RMB42.5 million to Jinjiang Xiaosheng and Jinjiang Menglang in 2006 and made a RMB1.0 million loan to 晉江電控設備有限公司 (Jinjiang Electricity Control Appliance Co., Ltd., or Jinjiang Electricity Control), an Independent Third Party, during the Track Record Period. Please refer to note 16 in section (C) of the Accountants' Report as set out in Appendix I to this document for further details of these cash advances and loans. All such cash advances and loans were unsecured, interest-free and had been repaid in full by 31 December 2007.

As advised by our PRC legal adviser, these cash advances and loans contravened certain regulations relating to bank financing in the PRC, particularly Lending Regulations (貸款通則) as promulgated by the PBOC. Our PRC legal adviser further advised that we may be subject to a penalty ranging from the amount of interest we received from a loan or cash advance made by us to five times the interest we received from a loan or cash advance made by us. In addition, we may be required to pay a penalty equal to prevailing lending rate charged by banks in the PRC on the amount of RMB1.4 million borrowed from Jinjiang Fengchuan Packing Co., Ltd. As advised by our PRC legal adviser, given that all the inter-enterprise loans and cash advances have been settled and that there has not been any legal disputes in respect of such loans or cash advances, the risk that we will be subject to penalties resulting from such loans or cash advances in contravention of PRC bank financing regulations is minimal.

In connection with such loans and cash advances, our Controlling Shareholders agreed to indemnify our Group in respect of any loss and liability that we may suffer as a result of any contravention of any PRC bank financing regulations, details of which are set out in "Appendix VI — Statutory and General Information — Other Information — Estate duty, tax and other indemnities".

In addition, in order to prevent any future non-compliance, we have ensured that all Directors are aware of the illegality of such advances/loans and will not allow any future advances or loans by or to our PRC subsidiaries in the PRC unless the advances or loans will be obtained from properly authorised banks or financial institutions and, in respect of any advances or loans to be made by our PRC subsidiaries, unless they will be made in a manner in compliance with the applicable PRC laws and regulations.

**Advances to certain related parties and third parties**

During the Track Record Period, we made advances or extended loans to certain related parties and third parties, including Fujian Strait and Jinjiang Electricity Control, (each an Independent Third Party), and Jinjiang Xiaosheng, Jinjiang Menglang and Messrs. Wang Dong Xing and Wang Cong Xing, (each a related party). These advances were primarily used to support the relevant parties' short-term working capital requirements (in the case of corporate entities) and short term financial needs (in the case of individuals). All of these advances/loans were properly approved by the relevant subsidiaries of our Company and documented in the form of payment request forms signed by a director or executed loan agreement. The principal of these advances, together with applicable accrued interest, had been repaid in full.

**No material changes**

Our Directors confirm that, up to the Latest Practicable Date, there has been no material changes in our Group's liquidity and financial resources and capital structure since 30 June 2009 which would materially affect the discussion and analysis contained in this section "—Liquidity and Capital Resources".

## INDEBTEDNESS

**Bank loans**

As at 31 December 2006, 2007 and 2008 and 30 June 2009, all of our bank loans were repayable within one year. Our bank loan agreements and related banking facility agreements contain covenants that are customary for PRC bank loans, including, among others, covenants requiring us to provide financial reports to the lenders and to notify the lenders (and in certain circumstances, obtain their prior consents) upon the occurrence of certain material events, and certain restrictions on our ability to provide guarantees, to dispose of assets and to distribute dividends. Other than a covenant requiring us to notify the lender upon the incurrence of material indebtedness and to obtain the lender's prior consent if such incurrence will adversely affect our ability to repay the related bank loan, none of the covenants contained in these agreements is expected to have a material impact on our ability to undertake additional debt or equity financings. Save as disclosed above, there is no other material covenant related to our outstanding debts.

As at 31 December 2006 and 2007, our bank loans of RMB125.5 million and RMB94.5 million were secured by personal guarantees granted by certain Directors and senior management of our Group. In addition, certain bank loans of approximately RMB5.5 million as at 31 December 2006 were secured by corporate guarantees granted by certain unrelated third parties. These corporate guarantees were released upon repayment of the bank loans in 2007. The personal guarantees granted by the Directors and senior management were released in April 2008.

In August 2009, Lilang International was granted by China Merchants Bank a six-month term loan facility in an amount of HK$15 million. Such loan facility was guaranteed by our Company and secured by a charge over bank deposits of Zhong Lee Development

Co., a private unlimited company established in Hong Kong and solely owned by Mr. Wang Cong Xing, our executive Director, which will be released or lapse upon the [●]. Funds borrowed pursuant to the short-term loan facility will be used as working capital for our Group. The facility bears a fixed interest rate of 3.60% per annum. We intend to use a portion of the proceeds from the [●] to repay such short-term loans made pursuant to this facility.

As at 31 July 2009, we had bank loans in the aggregate amount of RMB98.0 million.

Set forth below are the details of our bank loans and their respective effective interest rates:

| | As at 31 December | | | As at 30 June | As at 31 July |
|---|---|---|---|---|---|
| | 2006 | 2007 | 2008 | 2009 | 2009 |
| | *(RMB million)* | | | | |
| Fixed rate at 5.38%, 5.51%, 7.28%, 4.10% and 4.10% per annum at 31 December 2006, 2007 and 2008, 30 June 2009 and 31 July 2009 respectively | 80.5 | 54.5 | 100.0 | 77.0 | 77.0 |
| Floating rate at 5.81%, 6.72%, 5.31%, 5.31% and 5.31% per annum at 31 December 2006, 2007 and 2008, 30 June 2009 and 31 July 2009 respectively | 45.0 | 40.0 | 40.0 | 21.0 | 21.0 |
| | 125.5 | 94.5 | 140.0 | 98.0 | 98.0 |

**Amount due to related parties**

As at 31 December 2006, 2007 and 2008, 30 June 2009 and 31 July 2009, we owed RMB139.7 million, RMB139.4 million, RMB18.5 million, RMB10.9 million and RMB7.6 million, respectively, to the Wang Brothers or any of them, being our Controlling Shareholders and executive Directors. These amounts comprise a loan for an amount of approximately RMB139.4 million, which was of non-trade nature, unsecured, interest free and had no fixed repayment terms was granted by the Wang Brothers to our Group and the proceeds of the loan were used to fund the construction of our production facilities in the Wuli Industrial Park and our working capital. The entire amount of such loan in the aggregate amount of RMB139.4 million, has been capitalised as fully paid-up capital of our Company as part of the Reorganisation on 12 September 2008. All amounts due to the Controlling Shareholders or their respective associates have been repaid in full prior to the [●].

**No other outstanding indebtedness**

Except as disclosed above in this section "Indebtedness", we did not have outstanding mortgages, charges, debentures, loan capital, bank overdrafts, loans, debt securities or other similar indebtedness, finance leases or hire purchase commitments, liabilities under acceptances or acceptance credits or any guarantees outstanding as at 31 July 2009.

## CONTINGENT LIABILITIES

As at 31 December 2006, Lilang Fujian provided corporate guarantees to an independent third party, Jinjiang Shoe Enterprises Company Limited (晉江華意鞋業有限公司), or Jinjiang Shoe Enterprises, for its bank loans of RMB3.6 million, pursuant to a cross-guarantee arrangement with Jinjiang Shoe Enterprises which was terminated in October 2007. We have not recognised any deferred income in respect of the guarantee issued as its fair value cannot be reliably measured and the transaction price was not significant. During the Track Record Period, no claims had been made against us under the guarantees. The guarantees were released in October 2007.

We had no material contingent liabilities as at 31 July 2009. We are not involved in any current material legal proceedings, nor are we aware of any pending or potential material legal proceedings involving our Group.

## OFF-BALANCE SHEET ARRANGEMENTS

As at the Latest Practicable Date, we did not have any off-balance sheet arrangements or contingencies.

## NET CURRENT ASSETS

We had net current assets of RMB331.0 million as at 31 July 2009. Our current assets as at 31 July 2009 consisted of inventories of RMB193.8 million, trade and other receivables of RMB365.9 million, amounts due from shareholders of RMB17.6 million, pledged bank deposits of RMB25.4 million and cash of RMB82.4 million. Our current liabilities as at 31 July 2009 consisted of bank loans of RMB98.0 million, trade and other payables of RMB247.0 million, amount due to related parties of RMB7.6 million and current taxation of RMB1.6 million.

## CAPITAL EXPENDITURES

The following table sets out our historical capital expenditures during the Track Record Period:

| | Years ended 31 December | | | Six months ended 30 June |
|---|---|---|---|---|
| | 2006 | 2007 | 2008 | 2009 |
| | *(RMB million)* | | | |
| **Capital Expenditures** | | | | |
| Manufacturing, office and transportation equipment, leasehold improvement | 10.3 | 16.6 | 10.7 | 10.6 |
| Construction in progress | 12.7 | 58.9 | 32.2 | 5.5 |
| Land use rights | 19.6 | 4.4 | 6.8 | — |
| Investment property | — | — | 30.1 | 1.0 |
| Total | 42.6 | 79.9 | 79.8 | 17.1 |

Construction in progress represented capital expenditures for the construction of our production facilities in the Wuli Industrial Park. Land use rights represented expenditures for the purchase of land use rights for our production facilities in the Wuli Industrial Park and our planned research and product development facilities in Xiamen, Fujian province.

The following table sets forth our projected capital expenditures for the financial year ending 31 December 2009 which includes the construction in progress in connection with our product development facilities in Xiamen and product development center in Shanghai:

| | For the financial year ending 31 December 2009 |
|---|---|
| | *(RMB million)* |
| Manufacturing, office and transportation equipment, leasehold improvement | 108.7 |
| Construction in progress | 40.5 |
| Investment property | 1.0 |
| Total | 150.2 |

We expect to fund our capital expenditures principally with cash generated from our operations, bank loans and a portion of the net proceeds from the [●].

## COMMITMENTS

### Capital commitments

We had the following capital commitments outstanding at the dates indicated which were not provided for in our consolidated financial statements:

| | As at 31 December | | | As at 30 June |
|---|---|---|---|---|
| | 2006 | 2007 | 2008 | 2009 |
| | | *(RMB million)* | | |
| **Capital Commitments** | | | | |
| Contracted for | 50.6 | 14.5 | 5.5 | 0.4 |
| Authorised but not contracted for | 97.5 | 121.2 | 179.5 | 178.9 |
| Total | 148.1 | 135.7 | 185.0 | 179.3 |

These capital commitments primarily relate to plant, property and equipment purchases for the construction of our planned research and product development facilities in Xiamen, Fujian and our production facilities in the Wuli Industrial Park. Capital commitments as at 30 June 2009 also included capital commitments authorised but not contracted for the leasing of premises as flagship stores to our distributors in 2009 and 2010.

We expect to finance our contractual commitments that were outstanding as at 30 June 2009 principally with cash generated from our operations, bank loans and a portion of the net proceeds from the [●].

### Investment commitments

As at 31 December 2007 and 2008 and 30 June 2009, we had commitments in respect of contribution to investments in Lilang Xiamen, a wholly owned subsidiary of our Company, of approximately US$25.5 million (or approximately RMB175.0 million) which is due for contribution on or before 31 December 2009. These amounts are expected to be used to fund part of our outstanding capital commitments relating to plant, property and equipment purchases for the construction of our planned research and product development facilities in Xiamen, Fujian.

We expect to finance our investment commitments that were outstanding as at 30 June 2009 principally with our internal resources.

**Operating lease commitments**

We had the following future minimum lease payments payable under non-cancellable operating leases at the dates indicated:

| | As at 31 December | | | As at 30 June |
|---|---|---|---|---|
| | 2006 | 2007 | 2008 | 2009 |
| | | *(RMB million)* | | |
| **Operating lease commitments** | | | | |
| Within one year | — | — | 1.7 | 1.6 |
| Between one to five years | — | — | 0.3 | — |
| Total | — | — | 2.0 | 1.6 |

The operating lease commitments as at 30 June 2009 relate to lease agreements we entered into in 2008 and 2009 for our offices in Hong Kong, Jinjiang, Fujian and Xiamen and a production factory in Jinjiang, Fujian.

**INVENTORY ANALYSIS**

During the Track Record Period, inventories were one of the principal components of our current assets. The value of our inventories accounted for approximately 11.8%, 18.6%, 26.3% and 28.6% of our current assets as at 31 December 2006, 2007 and 2008 and 30 June 2009, respectively.

We closely monitor and control the inventory level of our raw materials and finished goods to optimise our operations. We limit the risks related to high inventory levels by planning our purchases and production and maintaining our stock of raw materials and finished goods by reference to the purchase orders received in sales fairs. We hold sales fairs three times a year to showcase styles for autumn, winter and spring/summer to our existing and potential distributors. In 2008, our sales fairs took place in March/April, May/June and August/September. For the six months ended 30 June 2009, our sales fairs took place in March/April and May/June 2009.

The following table is a summary of our balance of inventories as at the dates indicated:

| | As at 31 December | | | As at 30 June |
|---|---|---|---|---|
| | 2006 | 2007 | 2008 | 2009 |
| | | *(RMB million)* | | |
| **Inventories** | | | | |
| Raw materials | 13.5 | 20.3 | 18.4 | 40.3 |
| Work in progress | 2.7 | 1.2 | — | — |
| Finished goods | 24.1 | 74.5 | 153.1 | 145.7 |
| Total | 40.3 | 96.0 | 171.5 | 186.0 |

The following table sets out the average inventory turnover days for the Track Record Period:

| | Years ended 31 December | | | Six months ended 30 June |
|---|---|---|---|---|
| | 2006 | 2007 | 2008 | 2009 |
| Average inventory turnover days[(1)] | 32.4 | 38.2 | 61.7 | 76.0 |

(1) Average inventory turnover days is equal to the average inventory divided by costs of sales and multiplied by 365 days (180 days, in the case of the six months ended 30 June 2009). Average inventory equals inventory at the beginning of the year/period plus inventory at the end of the year/period and divided by two.

The increases in our inventories during the Track Record Period were attributable in part to increases in our sales during the same period. The increase in our inventories as at 31 December 2007 as compared to 31 December 2006 was also caused by the fact that the sales fair for the spring and summer collections in 2007 was held in October 2006, while the sales fair for the spring and summer collections in 2008 was held in September 2007. Though the date of our fair, and thus the date we received orders and began procuring products to fill such orders, was moved up one month, delivery of such products to distributors remained primarily in January and February. This resulted in higher inventory as at 31 December. Average inventory turnover days increased by 5.8 days from 2006 to 2007, primarily due to the above stated difference in the timing of the sales fair for the spring and summer collections in 2006 and 2007. Average inventory turnover days increased by 23.5 days from 2007 to 2008 primarily because the sales fairs in 2008 took place one month earlier than those in 2007. In addition, the follow-up orders placed by the distributors subsequent to the sales fairs were lower than expected prior to December 2008 which was due in part to the global economic condition which resulted in a higher inventory level in December 2008. In particular, during the second half of 2008, in anticipation of the potential impact of the financial crisis on the PRC economy, we implemented certain one-time measures where we recommended to distributors that they refrain from placing follow-up orders for the spring/summer season. For the six months ended 30 June 2009, average inventory turnover days increased by 14.3 days from 2008. For the six months ended 30 June 2008, average inventory turnover days was 63.1 days. Average inventory turnover days are typically higher as at 30 June (including those for 30 June 2008 and 2009) when compared to the average inventory turnover days as at 31 December (including those for 31 December 2008 and 2009) as the turnover is significantly higher in the second half of the year and we typically purchase more raw materials in the first half of the year in anticipation of higher sales in the second half of the year. The inventory turnover days for the six months ended 30 June 2009 was also higher due to the fact that we made a bulk purchase of raw materials because of attractive pricing offered by our suppliers.

We make specific provisions for obsolete or damaged inventories if the carrying amount of these inventories is lower than their net realisable value. For the years ended 31 December 2006, 2007 and 2008 and the six months ended 30 June 2009, provisions for inventories were approximately RMB2.3 million, RMB0.4 million, RMB2.2 million and RMB1.1 million, respectively. As at 30 June 2009, our inventories of 0 to 180 days, 181 to 365 days, and over 365 days were RMB178.5 million, RMB7.5 million and RMBnil million, respectively. Of the RMB186.0 million of inventories as at 30 June 2009, RMB72.2 million were subsequently used or sold during the one month ended 31 July 2009.

## TRADE AND OTHER RECEIVABLES

### Trade and bills receivables

Our trade and bills receivables primarily relate to receivables for goods sold to our distributors. Our agreements with distributors provide that our products will only be delivered to our distributors upon receipt of the payment for the products. However, we typically grant to our distributors credit periods of 60 days to 180 days depending on the circumstances, such as the distributor's credit history, repayment pattern and on-going relationship with us. See also "Business — Sales — Credit Policy."

The following table sets out an aging analysis of our trade and bills receivables at the dates indicated:

| | As at 31 December | | | As at 30 June |
|---|---|---|---|---|
| | 2006 | 2007 | 2008 | 2009 |
| | | *(RMB million)* | | |
| **Trade and bills receivables** | | | | |
| Within 3 months | 154.1 | 152.5 | 211.0 | 265.0 |
| Over 3 months to 6 months | — | 17.5 | 28.9 | 20.5 |
| Over 6 months to 1 year | — | 1.9 | 11.4 | 19.6 |
| Total | 154.1 | 171.9 | 251.3 | 305.1 |

Of the RMB305.1 million of trade and bills receivables as at 30 June 2009, RMB63.0 million were subsequently settled during the one month ended 31 July 2009.

Recently we have begun allowing our distributors in the PRC to use bank acceptance bills (which typically have credit terms of 60 to 120 days) to settle their purchases and trade receivables with us. These bills, once received by us, may be converted into cash prior to their maturity dates, subject to the payment of discount interest, or endorsed by us to settle our payables. These bills are issued by licensed banks registered in the PRC thereby substituting such banks' credit standing for that of the relevant distributors. Our bills receivable as of 31 December 2008 and 30 June 2009 were RMB1.6 million and RMB55.1 million.

The following tables sets out an aging analysis of trade and bills receivables that are neither individually nor collectively considered to be impaired:

| | As at 31 December | | | As at 30 June |
|---|---|---|---|---|
| | **2006** | **2007** | **2008** | **2009** |
| | | *(RMB million)* | | |
| **Trade and bills receivables** | | | | |
| Neither past due nor impaired | 154.1 | 152.5 | 207.8 | 268.3 |
| Less than 1 month past due | — | 13.6 | 22.7 | 10.8 |
| 1 to 3 months past due | — | 3.9 | 18.8 | 18.2 |
| More than 3 months past due | — | 1.9 | 2.0 | 7.8 |
| Subtotal | — | 19.4 | 43.5 | 36.8 |
| Total | 154.1 | 171.9 | 251.3 | 305.1 |

Trade and bills receivables that were neither past due nor impaired related to a wide range of distributors for whom there was no recent history of default. Trade receivables that were past due but not impaired related to a number of distributors that have a good track record of business relationships with our Group. Based on past experience, we believe that no impairment allowance is necessary in respect of these balances as there has not been a significant change in credit quality. All of the past due balances at 31 December 2006, 2007 and 2008 have subsequently been recovered. Our Group does not hold any collateral over these balances.

The following table sets out our average trade and bills receivables turnover days for the Track Record Period:

| | Years ended 31 December | | | Six months ended 30 June |
|---|---|---|---|---|
| | **2006** | **2007** | **2008** | **2009** |
| Average trade and bills receivables turnover days[(1)] | 61.8 | 57.4 | 58.1 | 71.3 |

(1) Average trade and bills receivables turnover days is equal to the average trade and bills receivables divided by turnover (plus value-added tax) and multiplied by 365 days (180 days, in the case of the six months ended 30 June 2009). Average trade and bills receivables is equal to trade and bills receivables at the beginning of the year/period plus trade and bills receivables at the end of the year/period and divided by two.

Average trade and bills receivables turnover days slightly decreased from 61.8 days in 2006 to 57.4 days in 2007 and increased to 58.1 days in 2008. Average trade and bills receivables turnover days was 71.3 days for the six months ended 30 June 2009. The average trade and bills receivables turnover days was 66.5 days for the six months ended 30 June 2008. The average trade and bills receivables turnover days is typically greater as at 30 June (including those for 30 June 2008 and 2009) when compared to 31 December (including those for 31 December 2008) as a large percentage of settlement of the orders placed by distributors subsequent to the sales fairs in May typically occurs in July and August (after the 30 June balance sheet date) while a substantial portion of orders placed by distributors subsequent to the sales fairs in September and October are typically settled prior to 31 December.

We have not had any significant bad or doubtful accounts or provided allowance for the same during the Track Record Period. For the years ended 31 December 2006, 2007 and 2008 and the six months ended 30 June 2009, no provision on bad or doubtful debts was required. In determining bad and doubtful debts, our management takes into account the credit history and payment pattern of our distributors together with their on-going relationship between us. We periodically review the payment status of our trade receivables and take appropriate measures to collect overdue accounts.

**Other receivables and prepayments**

Other receivables and prepayments mainly comprise prepayments to suppliers, prepaid advertising expenses, renovation subsidies and [●]. Prepayments to suppliers amounted to RMB51.5 million, RMB88.2 million, RMB98.8 million and RMB12.7 million as at 31 December 2006, 2007 and 2008 and 30 June 2009, respectively. Other receivables and prepayments, excluding prepayments to suppliers, amounted to RMB3.6 million, RMB45.2 million, RMB33.6 million and RMB24.0 million as at 31 December 2006, 2007 and 2008 and 30 June 2009, respectively. The increase of the balance as at 31 December 2007 compared to the balance as at 31 December 2006 was primarily due to our prepaid advertising expenses and renovation subsidies in the aggregate amount of RMB33.2 million recorded at 31 December 2007. The decrease in other receivables as at 31 December 2008 compared to as at 31 December 2007 was primarily due to completion of renovations on several retail outlets in 2008 and the resulting recognition of renovation subsidies relating to such retail outlets as selling expenses rather than other receivables. The decrease in other receivables as at 30 June 2009 was primarily due to a decrease in prepaid renovation subsidies and value added tax receivables.

*Prepaid advertising expenses and renovation subsidies.* Prepaid advertising expenses represent prepayments to our advertising agencies for advertising expenses. We do not make advertising subsidies to distributors. Prepayments for advertising expenses are recognised as expenses when the advertising programs are broadcasted. We generally make renovation subsidies to distributors and sub-distributors for their opening of new retail outlets and prepaid renovation subsidies represent prepayments made by us for store displays to be provided to distributors and sub-distributors as renovation subsidies. Prepayments for renovation subsidies are recognised as expenses when the renovation materials are delivered to distributors or sub-distributors. All distributors and sub-distributors opening new retail outlets can apply for renovation subsidies from us and whether renovation subsidies will be granted and the relevant amount will be determined by us based on factors such as the size and location of the new outlet.

We enter into written agreements with our advertising agencies and suppliers of renovation materials in respect of any such prepaid advertising expenses and prepayments for store renovation displays.

Our prepaid advertising expenses and renovation subsidies incurred during the years ended 31 December 2006, 2007 and 2008 and the six months ended 30 June 2009 were RMB3.0 million, RMB33.2 million, RMB4.1 million and RMB0.7 million, respectively.

## TRADE AND OTHER PAYABLES

### Trade and bills payables

Our trade and bills payables primarily relate to the purchase of raw materials and OEM products from our suppliers and advertising and promotional expenses, with credit terms of approximately 45 days for trade payables and three or six months for bills payables. Historically, our bills payables have generally been secured by pledged bank deposits and guaranteed by personal guarantees granted by certain Directors of our Company. The amount of bills payables guaranteed by personal guarantees from our Directors was RMB40.3 million, RMB149.5 million, RMBNil and RMBNil as at 31 December 2006, 2007 and 2008 and 30 June 2009, respectively. Such personal guarantees were released in April 2008.

The following table sets out our trade and bills payables by components during the Track Record Period:

| | As at 31 December | | | As at 30 June |
|---|---|---|---|---|
| | 2006 | 2007 | 2008 | 2009 |
| | | *(RMB million)* | | |
| **Trade and bills payables** | | | | |
| Trade payables | 19.6 | 38.0 | 51.1 | 70.0 |
| Bills payables | | | | |
| Purchase of materials and finished goods | 43.2 | 165.4 | 114.4 | 69.9 |
| Advertising and promotional expenses | — | 26.9 | 26.3 | 9.8 |
| Construction in progress | — | 3.0 | — | — |
| | 43.2 | 195.3 | 140.7 | 79.7 |
| Total | 62.8 | 233.3 | 191.8 | 149.7 |

The following table sets out an aging analysis of our trade and bills payable as at the dates indicated:

| | As at 31 December | | | As at 30 June |
|---|---|---|---|---|
| | 2006 | 2007 | 2008 | 2009 |
| | | *(RMB million)* | | |
| **Trade and bills payables** | | | | |
| Within 3 months | 49.9 | 225.8 | 137.8 | 133.2 |
| Over 3 months to 6 months | 10.2 | 3.5 | 50.3 | 5.4 |
| Over 6 months to 1 year | 0.9 | 1.2 | 2.7 | 8.5 |
| Over 1 year | 1.8 | 2.8 | 1.0 | 2.6 |
| Total | 62.8 | 233.3 | 191.8 | 149.7 |

During the years ended 31 December 2006, 2007 and 2008 and the six months ended 30 June 2009, the amount of trade and bills payables was RMB62.8 million, RMB233.3 million, RMB191.8 million and RMB149.7 million, respectively. Of the RMB149.7 million of trade and bills payables as at 30 June 2009, RMB59.2 million were subsequently settled during the one month ended 31 July 2009.

The following table sets out our average trade and bills payable turnover days for the Track Record Period:

| | Years ended 31 December | | | Six months ended 30 June |
|---|---|---|---|---|
| | 2006 | 2007 | 2008 | 2009 |
| Average trade and bills payable turnover days(1) | 47.6 | 74.5 | 85.0 | 64.9 |

(1) Average trade and bills payable turnover days is equal to the average trade and bills payable (excluding bills payables in relation to advertising and promotional expenses and construction in progress) divided by cost of sales and multiplied by 365 days (180 days, in the case of the six months ended 30 June 2009). Bills payables in relation to advertising and promotional expenses and construction in progress are excluded from this calculation because these expenses are not related to the determination of the average time between our purchases of raw materials and OEM products and their payment. Average trade and bills payable is equal to the trade and bills payable at the beginning of the year/period plus trade and bills payable at the end of the year/period and divided by two.

Our trade and bills payable level, primarily representing the purchase of raw materials used for our in-house production and OEM purchases, was relatively low as at 31 December 2006 primarily because of the fact that a smaller portion of our spring and summer collections for 2007 were produced before 31 December 2006. As a result, we purchased less amount of raw materials and OEM products during 2006, which led to a smaller amount of trade and bills payables being recorded as at 31 December 2006. Our trade and bills payable increased from 31 December 2006 to 31 December 2007 by approximately 271.6% primarily due to an increase in our purchase of raw materials and OEM products as a result of the increase in demand for our products. Our trade and bills payable decreased from 31 December 2007 to 31 December 2008 by approximately 17.8% primarily due to the fact that the 2008 spring/summer sales fair took place one month earlier than the one in 2007 resulting in a larger percentage of our purchases of raw materials being settled prior to 31 December 2008. Our trade and bills payable decreased from 31 December 2008 to 30 June 2009 by approximately 22.0% primarily due to the fact that the sales fairs for our autumn and winter collections took place in March/April and May/June and the raw materials purchased by us subsequent to the orders placed during the sales fairs were delivered by the suppliers in July and August 2009. As such, the level of the trade and bills payable was lower as at 30 June 2009. Average trade and bills payable turnover days increased from 47.6 days in 2006 to 74.5 days in 2007 and to 85.0 days in 2008, in each case, primarily because we utilised more bills payables, which have longer terms and therefore provide us with more liquidity than trade payables.

**Other payables**

Other payables mainly comprise accrued salaries and wages, payables for purchases of fixed assets, retirement benefit contributions payable, value added tax payables and receipts in advance for distributor orders. Our retirement benefit contributions payable increased from RMB3.0 million as at 31 December 2006, to RMB11.2 million as at 31 December 2007, to RMB21.7 million as at 31 December 2008, and then to RMB25.4 million as at 30 June

2009, primarily due to the increases in the number of employees to whom the payables were related. See "Business — Employment" for more information on our retirement benefits contributions.

## WORKING CAPITAL

Our Directors are of the opinion that, taking into consideration the financial resources presently available to our Group, including the cash generated from operations and the estimated net proceeds of the [●], our Group has sufficient working capital for its working capital requirements at least in the 12 months commencing from the date of this document.

## FINANCIAL RATIOS

For the years ended 31 December 2006, 2007 and 2008, our return on equity ratio, which is calculated as profit attributable to equity shareholders divided by average shareholders' equity, was approximately 101.2%, 99.3% and 52.7% respectively. The return on equity ratio during the years ended 31 December 2006 and 2007 were generally higher than that during the year ended 31 December 2008. The decrease in return on equity ratio was primarily due to the fact that the shareholders of our Company contributed additional capital in our Company in September 2008 which increased the shareholders' equity.

As at 31 December 2006, 2007 and 2008 and 30 June 2009, our total interest-bearing debt divided by total assets, was approximately 30.8%, 14.4%, 16.2% and 11.3%, respectively. See note 29(f) of "Appendix I — Accountants' Report" for details on the adjusted net debt-to-capital ratio.

As at 31 December 2006, 2007 and 2008 and 30 June 2009, our current ratio, which is calculated as current assets divided by current liabilities, was 1.6, 1.4, 1.6 and 2.0, respectively. Our current ratio decreased from 31 December 2006 to 31 December 2007, primarily due to an increase in our current liabilities, which was, in turn, principally caused by an increase in our investment in fixed assets in connection with the construction of our production facilities in the Wuli Industrial Park in Jinjiang, Fujian. Our current ratio increased from 31 December 2007 to 31 December 2008 primarily due to an increase in our current assets, which was, in turn, principally caused by (i) an increase in trade receivables in 2008 resulting from an increase in sales; and (ii) an increase in inventory level in 2008 which were partially offset by an increase in bank loans for our general working capital in 2008. Our current ratio increased further as at 30 June 2009, primarily due to an increase in our current assets, which was, in turn, principally caused by an increase in our cash and a decrease in bank loans resulting from the repayment of our bank loans.

## QUANTITATIVE AND QUALITATIVE INFORMATION ABOUT MARKET RISKS

We are exposed to credit, liquidity, interest rate and currency risks arising in the normal course of our business. These risks are limited by our financial management policies and practices described below.

**Credit risk**

Our credit risk is primarily attributable to cash and bank deposits and trade and other receivables.

Our cash and bank deposits are placed with major financial institutions and the credit risk related to these deposits is low.

Trade receivables are presented net of the allowance for bad and doubtful debts. These receivables are due within 60 to 180 days from the date of billing. Typically, we do not obtain collateral from distributors. We have a certain concentration of credit risk as approximately 33.5%, 11.5%, 12.2% and 12.2% and 60.0%, 31.7%, 24.7% and 33.7% of the total trade receivables were due from our largest customer and the five largest customers as at 31 December 2006, 2007 and 2008 and 30 June 2009, respectively.

We have a credit policy in place and our exposures to the credit risk related to trade receivables are monitored on an going basis. Our credit policy requires our sales and marketing department and our finance department to review the sales volume and past payment history of each distributor and propose the applicable credit terms, which will be reviewed and approved by our chief sales and marketing officer and a Director. Our credit policy also requires us to monitor the status of our trade and other receivables, including their aging and collection status, on a monthly basis. Management does not expect any significant credit risk related to trade receivables because all of our distributors have had an ongoing business relationship with us for a substantial amount of time and we monitor the risk related to our trade receivables in accordance with our credit policy and the operations of the distributors and sub-distributors closely by requesting and reviewing their weekly sales reports. All of our distributors have conformed to our policies and submitted the inventory and sales reports to us on a regular basis.

Our maximum exposure to credit risk is represented by the carrying amount of each financial asset in the consolidated balance sheets. As at 30 June 2009, we had cash of RMB94.3 million, pledged bank deposits of RMB27.8 million and trade and other receivables of RMB341.8 million. Except for the financial guarantees given by our Group as set forth in "Contingent Liabilities", our Group and our Company have not provided any other guarantees which would expose our Group or Company to credit risk.

**Liquidity risk**

Individual operating entities within our Group are responsible for their own cash management, including any short term investment of cash surpluses and the raising of loans to cover expected cash requirements. Our policy is to regularly monitor current and expected liquidity requirements by preparing and reviewing monthly cashflow forecasts for the following months and allocating cash uses and resources accordingly and our compliance with lending covenants (if any), to ensure that we maintain sufficient reserves of cash and adequate committed lines of funding from major financial institutions to meet our liquidity requirements in the short and longer term.

**Interest rate risk**

Except for bank deposits with stable interest rates, we have no other significant interest-bearing assets. We do not anticipate significant impact to interest-bearing assets resulting from changes in interest rates, because the interest rates of bank deposits are not expected to change significantly. Accordingly, our income and operating cash flows are substantially independent of changes in market interest rates. Details of the effective rates for bank deposits are disclosed in Notes 18 to our consolidated financial statements included in "Appendix I — Accountants' Report".

Our interest rate risk arises mainly from bank borrowings. Borrowings bearing variable rates expose us to cash flow interest rate risk. Borrowings bearing fixed rates expose us to fair value interest risk. We do not use derivative financial instruments to hedge our interest rate risk. See "— Indebtedness — Bank loans" for the interest rate and terms of repayments of our bank borrowings.

As at 31 December 2006, 2007 and 2008 and 30 June 2009, if interest rates on bank borrowings had been 100 basis points higher or lower with all other variables unchanged, our profit after taxation would have changed by approximately RMB329,000, RMB292,000, RMB300,000 and RMB158,000, respectively, mainly as a result of higher or lower interest expense on variable rate borrowings. The analysis above has been prepared assuming that the change in interest rates had occurred at the balance sheet date and had been applied to bank borrowings outstanding at that date. The 100 basis point increase or decrease represents our assessment of a reasonably possible change in interest rates over the Track Record Period and to the next balance sheet date. As at 30 June 2009, we had bank loans in the amount of RMB77.0 million carrying a fixed interest rate of 4.10% and bank loans in the amount of RMB21.0 million carrying a floating interest rate of 5.31%; as at 31 December 2008, we had bank loans in the amount of RMB100.0 million carrying a fixed interest rate of 7.28% and a bank loan in the amount of RMB40.0 million carrying a floating interest rate that was 5.31%; as at 31 December 2007, we had bank loans in the amount of RMB54.5 million carrying a fixed interest rate of 5.51% and a bank loan in the amount of RMB40.0 million carrying a floating interest rate that was 6.72%; as at 31 December 2006, we had bank loans in the amount of RMB80.5 million carrying a fixed interest rate of 5.38% and a bank loan in the amount of RMB45.0 million carrying a floating interest rate that was 5.81%.

**Foreign currency risk**

As most of our monetary assets and liabilities are denominated in Renminbi and we conduct our business transactions principally in Renminbi, our exchange rate risk is not significant and we do not employ any financial instruments for hedging purposes.

However, RMB is not a freely convertible currency and the PRC government may at its discretion restrict access to foreign currencies for current account transactions in the future. Changes in the foreign exchange control system may prevent the Group from satisfying sufficient foreign currency demands and the Group may not be able to pay dividends in foreign currencies to its shareholders.

See also note 29 to our consolidated financial statements included in the Accountants' Report in Appendix I to this document.

## DIVIDEND POLICY

Our Company declared a special cash dividend of RMB53 million in August 2009. Such special dividend had been paid to our then Shareholders on 20 and 21 August 2009. Save as disclosed above, no other dividends were paid by us or any of our subsidiaries to their then Shareholders during the Track Record Period. The payment and the amount of any dividends will depend on the results of our operations, cash flow, financial condition, statutory and regulatory restrictions on the payment of dividends, future prospects and other factors that we may consider relevant. Holders of the Shares will be entitled to receive such dividends on a pro rata basis according to the amounts paid up or credited as paid up on the Shares. The declaration, payment and amount of dividends will be subject to our discretion.

Dividends may be paid only out of our distributable profits as permitted under the relevant laws. To the extent profits are distributed as dividends, such profits will not be available to be reinvested in our operations. There can be no assurance that we will be able to declare or distribute any dividend in the amount set out in any of our plan or at all. Our dividend distribution record in the past may not be used as a reference or basis to determine the level of dividends that may be declared or paid by us in the future.

Subject to the factors described above, we currently intend to recommend at the annual general meetings of our Company dividends of approximately 30% to 50% of our net profit available for distribution to shareholders after the [●].

## RELATED PARTY TRANSACTIONS

With respect to the related parties transactions set out in Note 31 to our consolidated financial statements included in the Accountants' Report in Appendix I to this document, our Directors confirm that these transactions were conducted on normal commercial terms and/or that such terms were no less favourable to our Group than terms available to Independent Third Parties and were fair and reasonable and in the interest of our Shareholders as a whole.

For a discussion of related party transactions, see note 31 to our consolidated financial statements included in the Accountants' Report in Appendix I to this document.

## DISTRIBUTABLE RESERVES

As at 30 June 2009, we had distributable reserves in the amount of RMB468.2 million available for distribution to our shareholders. Our Company declared a special dividend of approximately RMB53.0 million in August 2009.

## PROFIT FORECAST

Our Directors believe that, in the absence of unforeseen circumstances and on the basis of the assumptions set out in "Appendix III — Profit Forecast", our Group's consolidated net profit attributable to the equity holders for the year ending 31 December 2009 is unlikely to be less than RMB[●] million (HK$[●] million).

On a pro forma basis and on the assumption that our Group had been listed since 1 January 2009 and a total of [●] shares were issued and outstanding during the entire year (taking no account of any shares which may be issued upon exercise of the [●], any options granted under the [●] Share Option Scheme or options that may be granted under the Share Option Scheme), the forecast earnings per share for the year ending 31 December 2009 is unlikely to be less than RMB[●] (HK$[●]).

## DISCLOSURE REQUIRED UNDER THE LISTING RULES

Our Directors have confirmed that as at the Latest Practicable Date, there are no circumstances which, had our Group been required to comply with Rules 13.13 to 13.19 in Chapter 13 of the Listing Rules, would have given rise to a disclosure requirement under Rules 13.13 to 13.19 of the Listing Rules.

## NO MATERIAL ADVERSE CHANGE

Our Directors confirm that, up to the Latest Practicable Date, there has been no material adverse change in the financial or trading position or prospects of our Group since 30 June 2009, and there has been no event since 30 June 2009 which would materially affect the information shown in the Accountants' Report set out in Appendix I to this document, in each case except as otherwise disclosed herein.