Management Discussion and Analysis

The year under review has been one in which the Group has delivered on the promises it made during the year for expansion in the China market. It has also been one in which, by acquiring distribution rights for Neutrogena products, the Group has successfully diversified its product range for the China market. The mode of the Group's major direct investment in China is now about to be replaced with a franchising model for future expansion. Hong Kong (together with Macau) continued to contribute around more than 50% of the Group's revenue for the year, due particularly to its successful beauty services business. The Group has worked hard to maximise returns from this mature and relatively stable market, while also adjusting its presence in Macau, Taiwan and Singapore to achieve optimum levels of market penetration based on the particular characteristics of each territory.

Overall results for the year under review have been very positive, with the Group enjoying a record high turnover. Excluding gains arising from changes in the fair value of investment properties, the Group's profit attributable to shareholders increased sharply to HK$13,600,000. Specifically, turnover from the Group's Hong Kong and Macau retail outlets increased over the previous year, while its beauty businesses continued to drive earnings. Within China, the profit contribution from the Group's ~H_2O+ operations represented a record high, and was double the profit contribution of the previous year.


strengthening
with collaboration

~H_2O+ Retail Business

China: new initiatives in a fast-growing market

The Group has continued to roll out new outlets ahead of schedule as part of the expansion of its ~H_2O+ retail presence in China. The number of outlets stood at 115 at the date of the Interim Report, and the Group is now already well on target to reach its stated goal by having 136 outlets operating by now. Having established a core group of self-owned ~H_2O+ stores in key cities in China, expansion is now primarily being driven by franchising arrangements with approved distributors, keeping further expansion costs low and minimising any associated risks.

Hong Kong: maintaining the best retail positioning

The Group's expansion plans are currently focused primarily in the China market, which offers extensive growth opportunities. Within Hong Kong and Macau, the Group is continuing to emphasis the importance of guaranteeing exposure in the best retail environment while optimising rental arrangements, and that has meant adjusting the locations of its stores where necessary. For instance, the Group's Log-On ~H_2O+ outlet in Taikooshing was closed in September 2006 but this was followed a month later by the opening of a new ~H_2O+ outlet in the nearby Jusco department store. Changes in the past year in Hong Kong have not significantly involved any reduction in the number of outlets operating, with the number of Hong Kong and Macau retail outlets remaining steady at 16.

Elsewhere in Asia: adjusting to changing realities

At year end, the Group operated four outlets in Singapore. As intimated in the Interim Report, it has become clear that ~H_2O+ department store outlets offer a better model for the Group's operations in Singapore than standalone stores. With this in mind, the Group expects to readjust its presence in Singapore in the coming year.

The economy in Taiwan, meanwhile, did not perform well in the past year and the political environment was unstable. As a result, the Group's business was affected. And the political strife there in late 2006 is expected to prolong the market downturn. The Group will continue outlet rationalisation in Taiwan to overcome market challenges in 2007.

Neutrogena Business

Neutrogena: diversification in the China context

The Group's involvement in distributing Neutrogena products in the China market, beginning from its agreement with Neutrogena's makers Johnson & Johnson in April 2006, has involved a rapid roll-out of outlets in China. Originally committed to having 40 outlets up and running by the end of 2006, as at the time of writing there are 41 in operation, 38 of those are directly operated by the Group. With this core selection of self-operated outlets in place, the Group expects most new outlets from now on to be operated on a franchise basis, which should result in further rapid growth in the number of outlets over the next few months. The franchise arrangement offers many benefits to the Group, including removing inventory and receivables risks, as all products are supplied to franchisees on a strictly cash-on-delivery basis.

Spa and Beauty Businesses

Spa and beauty businesses: positive profitability

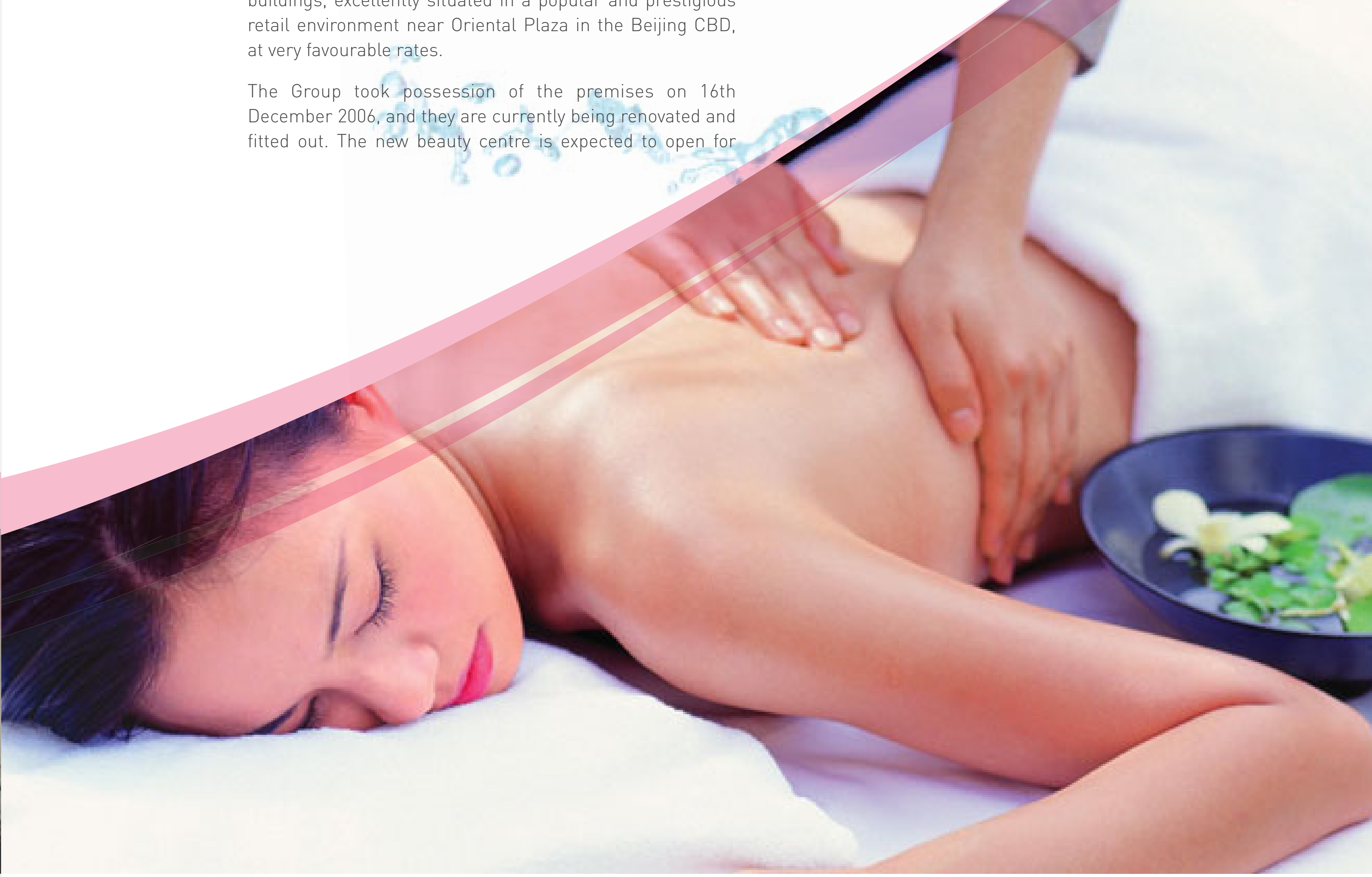
By mid-year, the Group's Oasis Spa business had turned around from a loss-making to a profit-making position. That strong run has continued right to the end of the fiscal year, supported by ongoing success of the Oasis Beauty chain. As a result, the spa and beauty side of the Group's overall business has contributed a solid 32% and over 40% of the Group's turnover and segment results respectively for the year.

The Group is now also ready to transplant its highly successful beauty centre model into the China market. Although originally intending to open its first beauty centre in Shanghai, the Group's flagship location will now be situated in Beijing. This reconsideration came about because the Group was offered a very attractive opportunity by a major Hong Kong developer, Sun Hung Kai. The developer invited the Group to become a tenant of one of its buildings, excellently situated in a popular and prestigious retail environment near Oriental Plaza in the Beijing CBD, at very favourable rates.

The Group took possession of the premises on 16th December 2006, and they are currently being renovated and fitted out. The new beauty centre is expected to open for business in April 2007. If the new beauty centre attracts a customer base according to forecasts, the Group targets to have a total of three beauty centres operational by the end of 2007. It is already exploring possible locations for further branches, including in Shanghai.

Oasis Beauty School

The Group's Oasis Beauty School continued its operations across the year, offering professional qualifications for those wishing to work in the beauty business. The School recorded a small loss for the year, but it continues to offer a value-added factor to the Group by giving access to high potential candidates for recruitment.



Prospects

Selected Oasis Beauty expansion

Latest assessment of the performance of the Group's beauty service centres has shown that some Oasis Beauty Centres in Hong Kong needed more capacity to meet demand during peak hours. Thus, the Group plans to integrate the three Sure Slim centres into the Oasis Beauty chain to achieve better economy of scale, more efficient use of management resources and to help cater for the increased demand in certain Oasis Beauty Centres. As certain facilities such as shower rooms, in existing Sure Slim centres are not available in most Oasis Beauty Centres, integrating Sure Slim into the Oasis Beauty chain will add value to the Group's beauty services.

Future growth for Neutrogena

The Group's involvement in distributing Neutrogena products began in early April 2006, and the latest figures (from October to December 2006) have already shown positive contributions from the existing (and still rapidly expanding) Neutrogena network in department stores in China. The Group expects this side of its business to begin contributing more significant profits in the coming fiscal year, particularly as it expands its franchise arrangements.

Using the franchise model, the Group has been pursuing an aggressive but carefully planned and realistic roll-out plan, and expects to have at least 120 Neutrogena counters in place by the end of 2007 in department stores in China. The brand's makers, Johnson & Johnson, have also committed themselves to providing more upmarket product lines from the US for distribution in China. These products, aimed at high-end customers, should further improve the Group's revenue generated from China.

Other opportunities

As reported earlier, the Group has already started renovation work for premises in Beijing where its first China beauty centre will be located. Renovations are currently underway, and the Group expects to begin operations by April 2007. Given its success in implementing the beauty centre concept in Hong Kong and its growing familiarity with the China market, the Group is optimistic that this new venture holds great promise. Indeed, as in Hong Kong, many customers in China will see the new beauty centre in Beijing as a natural extension of the Group's popular existing retail services. The Group already has a very considerable database of Oasis Club members in China, which it expects will provide the core of a wider wave of consumers looking for more upmarket beauty services than has been previously available. Because the market for quality beauty centres is still largely undeveloped in China, the Group believes there is huge potential for its growth within this sector.

At the same time, the Group will be introducing some exciting new ~H_2O+ products in the coming year that it expects will further boost the brand's reputation for quality and effectiveness. During 2007, almost every month will see the launch of a new ~H_2O+ product, including some new high-performance skincare products that are designed to work as integrated treatment series.

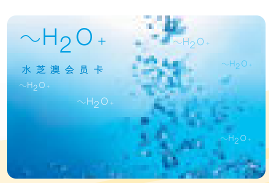
The Group also plans to launch a range of ~H_2O+ health drinks in the first half of 2007. These health drinks were initially sourced by Water Oasis from Japan, and have since been tested by H_2O Plus, L.P., in the United States and accorded ~H_2O+ branding. This product line represents the first ever ~H_2O+ health supplement product to come onto the market.

Positive macro-economic contexts

The announcement in early December 2006 that Hong Kong has abandoned possible plans to impose a GST represented good news for the Group along with the rest of the retail sector. Also at a macro level, the Group is aware of the possibility of benefits accruing to it if the RMB were to be allowed to appreciate in the coming year. As more and more of the Group's revenue originates from China, the potential of a strong RMB to boost the Group's profits is a very real one. For the year under review, 33% of the Group's total turnover originated from Mainland China, a 6% rise over the 27% recorded in the last fiscal year. With China's GDP predicted to rise sharply again in the coming year, prospects for the Group's China businesses look very positive.

Other

The group sold its Causeway Bay investment properties during the year ended 30th September 2006. Details of which has already been set out in the Company's circular to shareholders dated 7th April 2006 and the Group's 2006 Interim Report.



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