

Chairman's Statement

Dear Valued Shareholders,

On behalf of the board of directors of Lianhua Supermarket (the "Board"), I am delighted to present the annual report of the Group for the year ended 31 December 2006.

The Group continued to maintain its dominance as the largest supermarket chain and the largest fast-moving consumer goods chain in the PRC enterprise for ten consecutive years in terms of turnover. The Group achieved satisfactory performance in all its economic targets in 2006, with a strengthened and optimized network of better quality.

The implementation of various group policies by the government in the PRC ensured the rapid and healthy growth of the economy. According to the statistics by the National Bureau of Statistics of the PRC, in 2006, the PRC's gross domestic product ("GDP") grew



by 10.7% as compared to 2005, while the total retail sales of consumer goods in China increased by 13.7% as compared to 2005. Income of residents also recorded stable growth, and more importantly, the drive for economic growth has been gradually extending from central urban areas to rural areas, and as such, tremendous potential purchasing power is expectable.



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In light of the full-scale opening up of the PRC's retail market, competition became more intense. The Group adopted a more stable development approach to further focus on the expansion in high-potential regions while at the same time persisting in their nationwide development strategies, with an aim to realize its strategic objective of becoming the market leader in the regions. During the year under review, the Group further expanded its regional retail networks. All new outlets were located in the existing regions, with a net increase of 107 outlets (excluding outlets operated by associated companies). As at 31 December 2006, the number of outlets of the Group's three major brands reached 3,716 (excluding outlets operated by associated companies) in 20 provinces and municipalities such as Shanghai, Zhejiang, Jiangsu and Beijing, 81.08% of which are located in Eastern China.

While consolidating its developments, the Group has put greater emphasis on enhancing its internal management, catering for customers' specific needs, improving its supply chain system, optimizing internal management workflow and reducing operating costs. During the year under review, the Group recorded a turnover of approximately RMB16,446,967,000, representing an increase of approximately 14.91% from approximately RMB14,312,503,000 of the previous year. Profit attributable to shareholders also increased from approximately RMB239,677,000 last year by approximately 0.8% to approximately RMB241,599,000. Earnings per share was RMB0.39.

The Group has optimized its operating model through transformation, resulting in a model more adaptable to changes in market demands. Aggressive works have been carried out to transform the outlets of the Group to promote new growth with 85 outlets transformed during the year. As at



31 December 2006, the number of outlets which underwent transformation amounted to 95. Average daily sale of outlets which underwent transformation rose by approximately 23.26%, while the average purchase per transaction of customers increased by approximately 11.00% compared to the previous year, along with a rise in profit and customer satisfaction to the Group's transformed supermarkets. The Group is confident that such transformation will result in re-segmentation of the market as well as profit growth. The Group carried on the transformation of its supermarkets, and at the same time explored the feasibility of transformation for its hypermarkets and convenience stores. For instance, the Group actively conducted trial works in its Qingchun hypermarket in Hangzhou, Zhejiang Province, implemented a new design for the outlet, as well as introduced a variety of middle-to-high end fresh produce and other middle-to-high end goods to its product mix. Through transformation, daily sales of the Qingchun store rose by approximately 12.27% and the average purchase per transaction of customers increased by approximately 9.97% as compared to the corresponding period of last year.

During the year under review, the efficiency of the Group's supply chain was further enhanced. Leveraging on the supply chain management platform, retail order satisfaction rate rose by approximately 10%, effectively reducing the supply shortage of outlets and contributing to sales growth. For instance, through the use of the platform by Unilever China 聯合利華服務(合肥)有限公司 (hereinafter "Unilever China"), one of the Group's major suppliers, sale grew by approximately 24.96% as compared to the corresponding period of last year.

In response to the shareholder's staunch support, the Board recommends a payment of final dividend of RMB0.07 per share for the year ended 31 December 2006. Together with the interim dividend of RMB0.06 per share, the total dividends for the whole year will amount to RMB0.13 per share (2005: RMB0.13 per share).

Looking ahead, the Directors believe that the PRC's retail chain market will be filled with opportunities and challenges in a new era of great changes and competition. The opportunities will principally arise from strong and sustained economic growth, increasingly regulated policies and legal environment, as well as the Group's improving capability due to its outstanding market insight, pursuit of innovation, proactive transformation process and supply-chain development. The Group will adhere to its development mission and implement proper development approach to continuously strengthen its business in Shanghai and accelerate development in Eastern China in accordance with its nationwide expansion strategies. In order to realize higher profitability, the Group will continue to speed up its business transformation and innovation, improve the supply chain system development and consolidate a strong pool of talents so as to strengthen its leading position in the PRC's retail market and maximize shareholders' value.

On behalf of the Board, I would like to express my gratitude to our shareholders for their persistent trust and support for Lianhua Supermarket, and to our 40,000 employees for their strenuous efforts and valuable contribution to the long-term development of the Group.

By order of the Board



Wang Zong-nan
Chairman

18 April 2007
Shanghai, China





