CHAIRMAN'S Statement

> "We remain firmly committed to the growth of our business, to providing first-class customer services, to offering a best-in-class shopping experience for our customers, and to maintaining our position as a leading cosmetics retailer in the Asia-Pacific region."
>
> **Dr Simon Kwok**, *BBS, JP*
> Chairman and Chief Executive Officer

I hereby report that Sa Sa International Holdings Limited delivered a weaker performance for the year ended 31 March 2016 (the "fiscal year") despite the increasing number and intensity of challenges in the market. Over the past decade, our turnover and profit have steadily grown, reaching a new high in the last fiscal year. Currently, however, these results have shown a decrease due to strengthening headwinds.

Against the backdrop of weaker consumption sentiment and a continuing slowdown in growth of Mainland Chinese tourist spending, turnover reached HK$7,845.9 million, a decrease of 12.8%, while profit decreased by 54.3% to HK$383.5 million. Our footprint continued to expand, and our network now comprises 291 stores across the region.

The Group is committed to generating sustained and consistent returns to our shareholders. The Board of Directors proposes a final dividend of 9.0 HK cents per share and a special final dividend of 5.5 HK cents per share, making a total annual dividend for the fiscal year 23.5 HK cents per share after taking into account the interim dividend of 5.0 HK cents per share paid together with a special interim dividend of 4.0 HK cents per share. Subject to shareholders' approval, the final and special final dividends will be payable in cash with a scrip dividend alternative.

A Challenging Market Environment

In our core market of Hong Kong and Macau, retail sales have traditionally shown strong growth due to a high reliance on Mainland Chinese visitors, beginning with the launch of the Individual Traveller Scheme in 2003. However, this reliance has also led to our vulnerability in the Hong Kong retail market.

In recent times, political instability and anti-Mainland tourist sentiment have impacted the overall market in Hong Kong. Not only has there been a general slowdown in Mainland Chinese tourist arrivals, but also the pattern and profiles of these arrivals have changed. There has been a structural adjustment in the mix of shorthaul and longhaul tourists, of overnight and sameday tourists, and of their spending habits. In 2015, the one-visit-one-week permit imposed on Shenzhen residents for Hong Kong travel saw sameday visitor numbers fall on a year-to-year basis for the first time. Meanwhile Hong Kong's strong currency has undermined Hong Kong's competitive advantage, making it difficult to attract tourists for shopping while at the same time stimulating local outbound travel. Hong Kong's retail market will therefore continue to be under stress in the near term.

On the positive side, the Central Government has listed Macau tourism as a key sector for economic growth, which has given us grounds for optimism about our Macau market and its retail sector. Tourist facilities in Macau are now growing rapidly to attract and accommodate new tourists.

During the fiscal year, medicines and cosmetics sales in Hong Kong decreased 4.4% while the overall retail market declined by 6.4 %. During the same period, cosmetics and sanitary articles sales in Macau grew 11.4%, showing that the cosmetics industry remains comparatively resilient in that market. Overall, our sales and profitability have weakened, with our retail sales in Hong Kong and Macau decreasing by 14.2%. In general, we have underperformed the market and we are determined to adopt robust measures to adapt to market changes and boost our relative performance.

Drawing on our experience and our prediction of market trends, we are realigning our business operations to implement a more cautious store opening strategy and consolidating our network to be more sales and cost effective. We are centralising and streamlining work processes to improve operational and cost effectiveness as well as to enhance store productivity.

Furthermore, we are re-mapping our product strategy and execution with an emphasis on agility, effectiveness and efficiency. These measures will help us to embrace growing demand and allow us to recapture our robust sales growth trajectory. To enhance the competitiveness of our product portfolio, we will eliminate underperforming SKUs to make way for new and productive SKUs. We will also focus on the launch time of new products, as well as on their display, variety and pricing.

Beyond Hong Kong and Macau

In addition to addressing the difficult Hong Kong retail environment, the Group has been strategically adjusting our direction in our non-Hong Kong markets. We have placed more emphasis on e-commerce and we have begun to integrate our online and offline operations ("O2O") to increase competitiveness, to provide a better O2O shopping experience to customers, and to serve mainland tourists after they have left Hong Kong to return to their home base.

We have also devoted more critical analysis to assessing the profitability and efficiency of our non-Hong Kong markets' operations. We have reformed the management structure in several markets, improved scalability due to personnel and execution issues by investing in business processes and automation, and made a determined effort to build our base for future growth outside of our Hong Kong core market.

In Mainland China, we have continued to adjust our strategies to adapt to this important and evolving market. We have reformed the management team, accelerated O2O business development to tap growth in the market in line with government directions, and launched our new boutique store format.

In Malaysia, we have broadened our customer base to target the ethnic Malay population, and expanded our store network. In Singapore, we have successfully restructured our management team and operations, and we have begun to reap the benefits of integrating our Singapore with our Malaysia team. In Taiwan, we are focusing on upgrading our operations.

In our e-commerce business, we have fully recognised that understanding the behaviour and fulfilling the needs and habits of Chinese consumers are vital to drive our future growth. We have enhanced customer engagement and committed ourselves to increasing resources to improve the customer shopping experience, to enhance our product offerings, and to strengthen our marketing effectiveness. It is our belief that business and operations' scalability is vital to support growth. We have invested in human resources and our knowledge base to improve our competitive edge and help us drive the expansion of our business. Our online team in Hong Kong and Mainland China has grown not only in numerical terms but also in capability strength.

Road Map to the Future

We believe that the fiscal year of 2016/17 will be a difficult one for the Hong Kong retail market and will present many challenges. Nevertheless, we also believe that Hong Kong will continue to enjoy the advantages of being adjacent to economically robust southern China. Looking forward, therefore, the Group aims to further strengthen our competitiveness through the following measures.

In terms of product strategy, our product portfolio will be streamlined to allow us to better manage our inventory, reduce carrying costs, and make way for new and more productive products with better shelf display. The sourcing strategy and process will be improved to introduce popular new products, and we will target fast moving new and trendy products in order to achieve more rapid turnover. In view of the popularity of Korean cosmetic products, and to cater for rapidly changing customer preferences, we are enriching our Korean product portfolio across all product sources, including house brands and non-house brands. We will forge close partnerships with suppliers and Korean beauty brands while continuing to enhance branding and marketing initiatives for our owned brands, thereby contributing to the profit margin of the Group.

Overall, we will focus on retail network rationalisation, increasing store productivity and reducing operating costs, including rental costs. The streamlining of SKUs will allow us to enhance store productivity by removing unproductive SKUs and will also make it easier to display new and productive SKUs. The centralisation of operations will enable us to reduce costs at the store level. We are placing more emphasis on locations that will deliver continuous growth for targeted store expansion, such as the New Territories districts near the Mainland border. At the same time, we are rationalising our stores in those tourist districts in which "Sasa" stores are concentrated as a result of rapid growth over the past decade, such as Causeway Bay, Tsim Sha Tsui and Mongkok. These efforts will allow us to streamline our costs' structure and improve store productivity.

We also aim to drive sales through market differentiation. New store formats such as Sa Sa Boutique and SHINE will target different customer segments while also increasing market share, particularly for the local segment. In terms of O2O and cross-border e-commerce, we will drive sales growth through greater efforts in digital marketing and in the integration of our online and offline CRM. These measures will ensure an improved shopping experience. They will also allow us to maintain closer contact with our customers and to serve them even if they do not return regularly to Hong Kong. Customer acquisition and retention will both enhance and drive sales growth, and we will further strengthen sales channels through new and closer partnerships.

Service excellence has always been Sa Sa's number one core value. Our service has helped us to build relationships and trust with local and overseas customers while also strengthening Sa Sa as a top-of-the-mind brand in the market. To respond to the rapid changes in the market environment, our training, incentives and services are all evolving to cater for fresh product offerings that align with developments in consumer preferences – both in terms of product affinity and shopping experience. We recognise that the provision of an excellent shopping experience that consumers truly enjoy is essential and involves both online and offline efforts. We are therefore making sustained efforts to integrate our online and offline CRM, improve digital marketing, and also enhance our product offerings and store displays.

Realising our Vision

We aim to respond to forthcoming market challenges with flexibility and decisiveness, and to expand according to a strategy that is both disciplined and forward thinking. We are cautious on the short-term outlook but are optimistic about the long-term sustainability of our business, not just in our Hong Kong stores, but also for both the offline and online environments and throughout the region. We base this optimism on the fast-growing Mainland Chinese middle class whose levels of affluence will steadily rise, and who will continue to increase their spending. Hong Kong will also become further integrated into China through enhanced transportation infrastructure such as the high-speed rail link and the Hong Kong-Zhuhai-Macau bridge.

As mentioned above, we will strenuously improve our store operations and cost structure and improve our product strategy as well as operations to adapt to keen competition, changes in consumer behaviour, and the general weakness in the retail market. We are confident that the increasing integration of our O2O operations will better serve our customers and provide a shopping experience that will increase our customer base, reinforce customer loyalty, and drive sales. Leveraging on the solid foundation and experience of our Hong Kong core market, the Group is committed to strengthening the operations of our overseas markets. We aim to achieve growth in sales and market share while fine-tuning our strategic development to cater to the local market conditions of each respective market, and to increase their proportionate contribution.

Going forward, we will continue to invest in standardising, streamlining and automating operational and business processes, using IT technology to increase efficiency and control throughout the Group, in order to sustain growth now and in the future.

Finally, as the Group expands and grows, our commitments as a socially responsible corporate citizen continue to motivate us and to offer an ongoing source of satisfaction. We are proud to have accelerated our programmes in this area as we embrace our belief in "from the community, for the community", which we strongly believe is the key to sustainable business success.

Conclusion

I would like to take this opportunity to express my heartfelt gratitude to everyone who has contributed to the Group's performance and long-term sustainable growth. Whatever challenges Sa Sa may encounter in the future, I firmly believe that the Group's financial robustness, our strong governance and development strategies, and our flexibility and resilience, will ensure that we are able to overcome them. For many years the Group has shown strength and resourcefulness in all economic circumstances. We remain firmly committed to the growth of our business, to providing first-class customer services, to offering a best-in-class shopping experience for our customers, and to maintaining our position as a leading cosmetics retailer in the Asia-Pacific region.

Dr Simon Kwok, *BBS, JP*
Chairman and Chief Executive Officer
Hong Kong, 23 June 2016

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