
INDUSTRY OVERVIEW

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INDUSTRY HIGHLIGHTS

Consumer retailing in the PRC is generally affected by the size and purchasing power of the population concerned.

The PRC has been one of the world's fastest growing economies in the past decade, and has presented ample sales and marketing opportunities for the distributors of consumer goods. According to the National Bureau of Statistics of China, the PRC population reached approximately 1.31 billion at the end of 2005, with an urbanization rate of 43.0%. The GDP increased from approximately RMB5.8 trillion in 1995 to approximately RMB20.9 trillion in 2006. In light of the growth in population and urbanization rate, the Directors anticipate that there are tremendous opportunities for the development of the consumer goods industry in the PRC.

The Beijing population is one of the most affluent groups in the PRC in terms of residents' disposable income. The per capita annual disposable income of the urban residents of Beijing was RMB19,978 in 2006. The per capita annual consumption expenditure of the urban residents of Beijing was RMB14,825 in 2006.

In addition, Beijing will host the Olympic Games in 2008. It is expected that the increasing tourism and the commencement of various infra-structure projects in connection with the hosting of the Olympic Games will continue to stimulate economic growth and consumption in Beijing and the surrounding areas, creating continual growth opportunities for distributors of consumer goods.

Furthermore, the growth in population, disposable income and living expenditure in Beijing will similarly provide ample business and marketing opportunities for the distributors of consumer goods. Retail sales of consumer goods in Beijing increased from approximately RMB95.0 billion in 1995 to approximately RMB327.5 billion in 2006.

As a result of the PRC's accession to the WTO, the PRC chain store industry was significantly less regulated in terms of shareholding restriction and location restriction. This is expected to lead to the rapid growth of the consumer goods industry as foreign retailers enter the PRC market. In this respect, the Directors believe that the growth of the consumer goods industry would continue as a result of the rapid growth of the PRC population, disposable income and living expenditure.

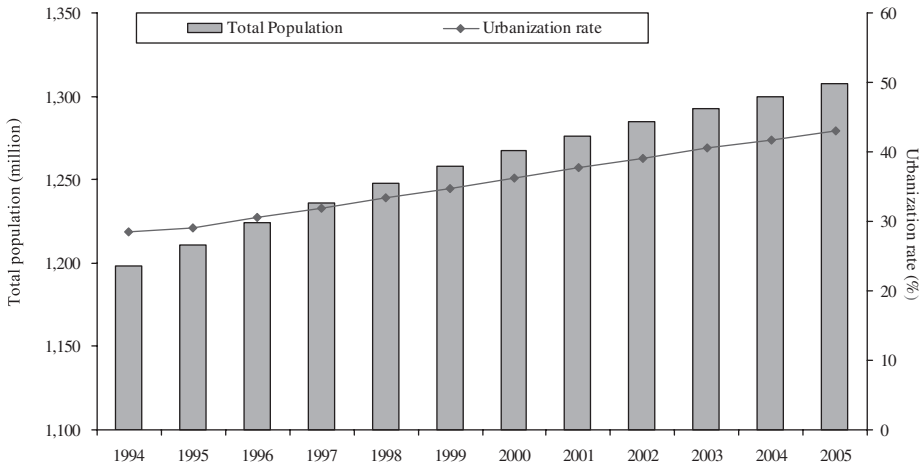
The economy of the PRC

Consumer retailing in the PRC is generally affected by the size and purchasing power of the population concerned.

INDUSTRY OVERVIEW

The population of the PRC has grown continuously during the past decade. According to the National Bureau of Statistics of China, the PRC population reached approximately 1.31 billion at the end of 2005 while urbanization rate reached 43.0%. In light of the growth in population and urbanization rate, the Directors anticipate that there are tremendous opportunities for the development of the retail industry in the PRC. The chart below illustrates the growth in population and urbanization rate in the PRC during 1995-2005:

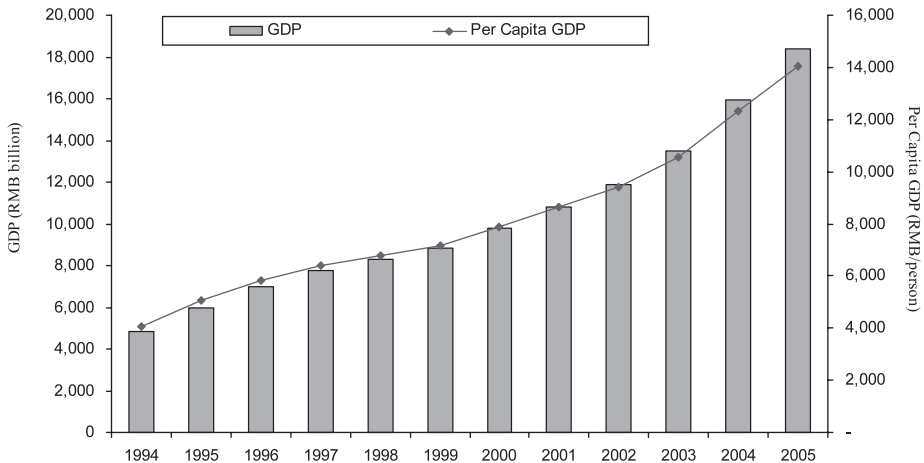
The growth in population and urbanization rate of the PRC



Source: National Bureau of Statistics of China

The PRC has been one of the world's fastest growing economies in the past decade. Its GDP increased from approximately RMB5.8 trillion in 1995 to approximately RMB20.9 trillion in 2006. The GDP per capita increased from approximately RMB5,046 in 1995 to approximately RMB14,040 in 2005, representing a CAGR of approximately 10.8%.

The growth in GDP and Per Capita GDP of the PRC

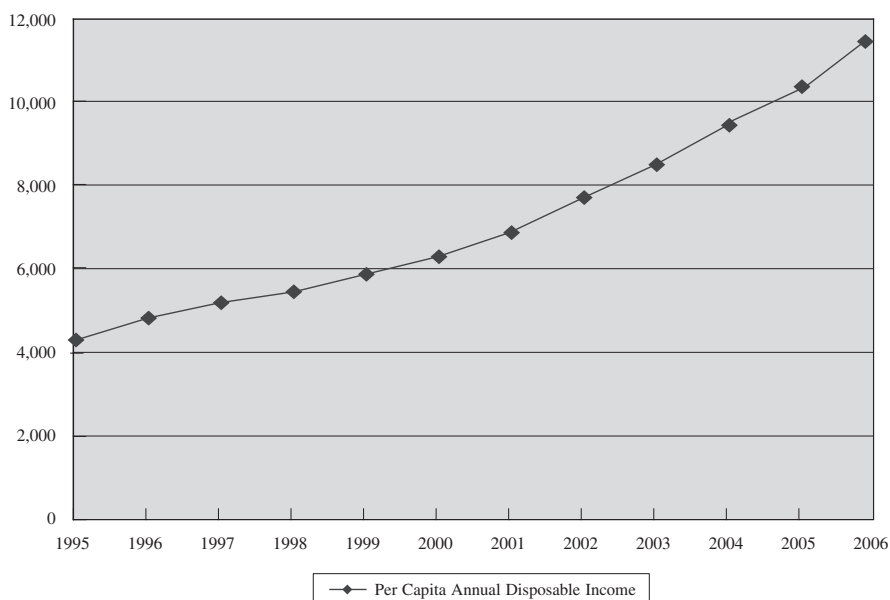


Source: National Bureau of Statistics of China

INDUSTRY OVERVIEW

The strong economic growth of the PRC has led to an improvement in living standards, in particular for those in the urban areas. According to the National Bureau of Statistics of China, the per capita annual disposable income of urban households increased from approximately RMB4,283 in 1995 to approximately RMB11,759 in 2006.

Per Capita Annual Disposable Income of Urban Households of the PRC



Source: National Bureau of Statistics of China

The economy of Beijing

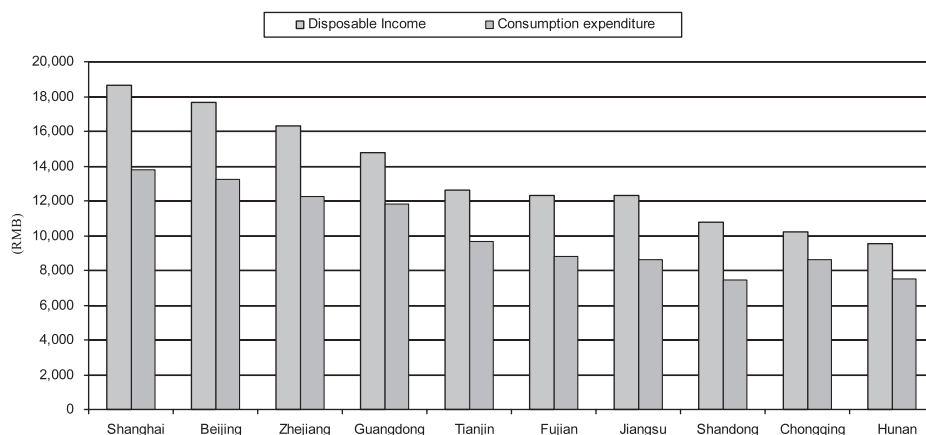
Beijing is the capital of the PRC and is one of the most populated cities of the country. According to the Beijing Municipal Bureau of Statistics, the population of Beijing increased from approximately 12.51 million in 1995 to approximately 15.81 million in 2006.

Beijing will host the Olympic Games in 2008. It is expected that the increasing tourism and various infra-structure projects for the Olympic Games will continue to stimulate economic growth and consumption in Beijing and the surrounding areas.

The Beijing population is one of the most affluent groups in the PRC in terms of the residents' disposable income. The per capita annual disposable income of urban residents of Beijing was RMB19,978 in 2006, which was second highest within the country. The per capita annual consumption expenditure of urban residents of Beijing was RMB14,825 in 2006, the second highest within the country.

INDUSTRY OVERVIEW

Per Capita Annual Disposable Income and Per Capita (Annual Consumption Expenditure) of Urban Residents of regions in the PRC in 2005



Source: National Bureau of Statistics of China

The growth in population, disposable income and consumption expenditure in Beijing has provided ample business opportunities for the retail business sector. Retail sales of consumer goods in Beijing increased from approximately RMB95.0 billion in 1995 to approximately RMB327.5 billion in 2006.

The economy of the Chaoyang District

The Chaoyang District is located in eastern Beijing, covering 455.08 square km and having a population of approximately 2.5 million.

The Chaoyang District is the window of Beijing. Being the central business district of Beijing, more than 90 percent of foreign embassies and majority of the city's five star hotels are located in the Chaoyang District. Major facilities in the district include the Beijing Capital Airport, Beijing Workers' Stadium and Asian Games Village.

The Chaoyang District is one of the largest and most populated districts in Beijing. The residents of Chaoyang are among the most affluent groups in Beijing. The high-income population provides ample business opportunities for retail chain operators. The table below illustrates the number and annual remuneration of employed persons of the Chaoyang District as compared to the other districts in Beijing:

INDUSTRY OVERVIEW

Number of employed persons and annual remuneration of districts in Beijing in 2005

District	Number of employed persons ('000)	Annual remuneration (RMB million)
海淀區 (Haidian)	984	35,314
朝陽區 (Chaoyang)	840	35,489
西城區 (Xicheng)	583	24,075
豐台區 (Fengtai)	439	11,100
東城區 (Dongcheng)	435	17,039
宣武區 (Xuanwu)	241	8,295
順義區 (Shunyi)	220	5,883
大興區 (Daxing)	211	5,727
昌平區 (Changping)	197	4,570
通州區 (Tongzhou)	182	3,198
石景山區 (Shijingshan)	160	4,855
房山區 (Fangshan)	132	3,050
崇文區 (Chongwen)	103	3,008
密雲縣 (Miyun)	79	1,552
平谷區 (Pinggu)	74	1,306
懷柔區 (Huairou)	64	1,634
門頭溝區 (Mentougou)	62	1,437
延慶縣 (Yanqing)	40	944

Source: Beijing Municipal Bureau of Statistics

Number of employed persons and annual average wage of selected regions in the PRC in 2005

District	Number of employed persons ('000)	Annual average wage (RMB)
北京 (Beijing)	5,056	34,191
上海 (Shanghai)	3,332	34,345
廣東 (Guangdong)	9,043	23,959

Source: National Bureau of Statistics of China

Beijing's success in the bid for the 2008 Olympic Games has provided the city and particularly the Chaoyang District with great opportunities for development. The Olympic Green, located in the Wali and Datun area in north Chaoyang, covers 12.15 square km. The construction of the central business district and the Olympic Green will greatly expedite the process of the urbanization of rural Chaoyang, the modernization of urban areas and internationalization of the district as a whole.

INDUSTRY OVERVIEW

THE PRC RETAIL INDUSTRY

With the largest population of the world and a rapid economic growth, the retail market in the PRC presents immense sales and marketing opportunities for distributors of consumer goods. The increase in personal wealth and purchasing power for the majority of the people in the PRC has also led to an expansion of retail business in the PRC in the past ten years.

The different formats of retail distribution of daily consumer products in the PRC are characterised by their location, size, decoration of stores, target customers, types of merchandise and operating styles. The primary retail formats that have been established include hypermarkets, supermarkets and convenience stores. The table below show key features of these retail formats.

Classification	Location	Size	Merchandise
Hypermarket	Commercial districts at main traffic junctions	Over 6,000 m ²	Clothings, food and beverages, household goods
Supermarket	Residential and commercial districts	Less than 6,000 m ²	Packaged food, fresh food products and household goods
Convenience store	Commercial districts, high traffic volume areas, public facilities such as bus stations, hospitals, schools, entertainment facilities, office buildings and gas stations	Around 100 m ²	Instant food, drinks and groceries

Source: MOC – 2004

Chain stores in the PRC

Prior to the PRC's accession to the WTO, the PRC chain store industry was strictly regulated in terms of shareholding restriction and location restriction. However, after 11 December 2004, wholly-foreign owned investment in retail sector is permitted and most restrictions on location and number of outlets have been removed. It is expected that foreign retailers will further penetrate the PRC retail industry in the future. The entry of large foreign chain store groups is expected to intensify competition and speed up the modernization of the industry.

Large retail chain operators in the PRC enjoyed substantial growth in the previous years. The sales of the top 100 retail chain operators accounted for an increasing portion of the total retail sales of consumer goods in the PRC each year from 2000 to 2006. The table below sets out the growth in retail sales of consumer goods and sales of the top 100 chain store operators in the PRC during such period.

INDUSTRY OVERVIEW

Retail sales of consumer goods and sales by the top 100 retail chain operators in the PRC

Year	2001	2002	2003	2004	2005	2006
Sales of the top 100 retail chain operators (RMB billion)	162	247	358	497	708	855.2
Growth rate	65%	52%	45%	39%	42%	25%
Annual growth of retail sales of consumer goods	10.1%	10.2%	9.2%	10.2%	12.9%	13.7%
Percentage of sales of the top 100 retail chain operators comprising the retail sales of consumer goods	4.3%	6.0%	7.8%	9.3%	10.5%	11.2%

Source: China Chain Store & Franchise Association

The Directors believed that the growth of the retail chain store industry would continue as a result of the growth of the PRC economy. With the intense competition from the foreign operators, the Directors expect that (i) Chinese retail chain operators will converge their supply chains and create their proprietary brands; (ii) some large Chinese retail chain operators will reposition themselves and co-operations with international retail chain operators are expected; and (iii) retail chain operators, particularly supermarket chain operators, will carry out greater assets and resources integration.

Retail chains in Beijing

Beijing is one of the PRC cities where retail chains have a high penetration rate. According to the China Chain Store & Franchise Association, by the end of 2005, the number of chain stores in Beijing reached 5,973. The sales by retail chains in Beijing for 2004 increased by 32.6%, as compared to that for the previous year, and accounted for approximately 29% of total retail sales of daily consumer products in Beijing. The table below sets out the top supermarket chain operators in Beijing in terms of sales in 2006.

Top Supermarket Chain Operators in Beijing in 2006

	Types of Retail Outlets	Number	(Sales of Retail Outlets in RMB million)
物美集團 (Wumart Group) (including 北京美廉美 (Beijing Mei Lian Mei))	Hypermarkets/Supermarkets/ Convenience Stores	751	25,520
北京京客隆 (Beijing Jingkelong)	Hypermarkets/Supermarkets/ Convenience Stores	171	6,134 ⁽¹⁾
北京超市發 (Beijing Chao Shi Fa)	Supermarkets	51	1,681
北京順天府 (Beijing Shun Tian Fu)	Supermarkets	20	992

Source: China Chain Store & Franchise Association

Note:

- (1) The figure reported by the China Chain Store & Franchise Association represents the aggregated sales of members of the Group before any elimination of intra-group transactions, audit adjustments and GAAP adjustments. Therefore the figure is not the same as the consolidated revenue amount appears in Appendix I to this document.

INDUSTRY OVERVIEW

Laws and regulations concerning the PRC retail industry

Pursuant to applicable PRC laws, operators of hypermarkets, supermarkets and convenience chain stores are required to obtain various permits and licences from certain PRC government authorities such as licences include:

1. hygiene permit
2. permit for tobacco monopoly retail business
3. permit for circulation of publications
4. animal quarantine permit

The PRC had started to progressively admit foreign-invested entities to the country's retail market since early 1990s. In 1992, the State Council stipulated the qualifying conditions for foreign investment in commercial retail enterprises by promulgating the guidelines on 《關於商業零售領域利用外資問題的批覆》 (Approval Regarding Foreign Investments in the Commercial Retail Industry) and permitted trial operation of certain foreign investment commercial enterprises in six major cities (including Beijing and five Special Economic Zones).

《中華人民共和國反不正當競爭法》 (The PRC Law Against Unfair Competition), which was promulgated in 1993, states that business operators are not permitted to sell commodities below cost for the purpose of eliminating competition. Only the following shall not be deemed as unfair competition acts: (1) sale of live commodities; (2) disposal of commodities near their expiration dates, or inventory that have been held for a long period of time; (3) seasonal sales; and (4) sale of commodities at a reduced price for the purpose of clearing off debts, change of business or suspension of operation. Violation of this regulation renders the offender liable to compensate losses suffered by other business operators.

In June 1998, the State Internal Trade Bureau promulgated 《零售業態分類規範意見(試行)》 (the Opinion Regarding Standardization of Retailing Business Classification (Provisional)), which clearly defines, for the first time, various types of retail business such as department stores, supermarkets and hypermarkets.

Pursuant to 《外商投資商業領域管理辦法》 (the Administrative Rules on Foreign Investments in Business Areas) promulgated in April 2004 by the Ministry of Commerce, any foreign investor who has acquired a good reputation and has never been acting in such manner that was in breach of any laws, administrative regulations and relevant rules in the PRC may establish a foreign-owned business enterprise and open retail outlets for business, subject to prior approval by relevant department on commercial affairs, as well as the registration requirement by the relevant administrating institutions.

Pursuant to the notice regarding full implementation of the State standard of 《零售業態分類》 (Retail Industry Classification) in August 2004 by the Ministry of Commerce, the retail industry has been categorised into 17 formats such as eatery, convenience store, discount shop, supermarket, hypermarket, department store and specialty store, etc.

Pursuant to the Administrative Rules on Franchise Business Operations promulgated in December 2004 by the Ministry of Commerce, a foreign enterprise shall extend its scope of business to include "business operation in franchise mode" in order to be allowed to conduct operations in a franchising format.