联华超市股份有限公司
**LIANHUA SUPERMARKET HOLDINGS CO., LTD.**

*(a joint stock limited company incorporated in the People's Republic of China with limited liability)*

**(Stock Code: 00980)**

# ANNOUNCEMENT OF RESULTS FOR THE YEAR ENDED 31 DECEMBER 2013 AND APPOINTMENT OF DEPUTY GENERAL MANAGER

## FINANCIAL HIGHLIGHTS

In 2013, China's economy recorded continuous growth with significant structural changes, imposing huge influence on the chain supermarket industry. The Group made active efforts in business transformation and upgrade in response to the ever-increasing fierce market competition, constant rising costs and changing structure of demand. As at 31 December 2013, the Group recorded the following:

- Turnover amounted to RMB30.38 billion, representing a growth of 4.8% over 2012. The same store sales of the Group grew by approximately 2.13% over 2012, in which hypermarket segment grew by approximately 1.22%, supermarket segment grew by approximately 2.61% and convenience store segment grew by approximately 11.13%.
- Gross profit amounted to approximately RMB4.36 billion, representing an increase of approximately 11.0% over 2012. Gross profit margin was approximately 14.36%, recording an increase of 0.81 percentage point over that of 2012.
- Distribution expenses and administrative expenses totalled approximately RMB6.92 billion, of which labor cost and rental cost increased rigidly. Overall cost ratio kept stable over 2012.
- Consolidated income amounted to approximately RMB7.30 billion, representing an increase of approximately 2.0% over 2012. Consolidated income margin was approximately 24.02%, decreasing by 0.66 percentage point over that of 2012.
- Operating profit amounted to approximately RMB0.27 billion, representing a decrease of 48.1% over 2012. Profit attributable to shareholders of the Company amounted to RMB0.05 billion. Basic earnings per share were approximately RMB0.05.
- The total number of outlets reached 4,530. During the period under review, the Group opened 312 new outlets, including 3 newly-opened hypermarkets, 153 newly-opened supermarkets (including 21 directly-operated stores and 132 franchised stores), 156 newly-opened convenience stores (including 52 directly-operated stores and 104 franchised stores).

*Note 1:* Consolidated income = Gross profit + Other revenues + Other income

*Note 2:* Consolidated income margin = (Gross profit + Other revenues + Other income)/Turnover

**CONSOLIDATED STATEMENT OF PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME**
*FOR THE YEAR ENDED 31 DECEMBER 2013*

| | *NOTES* | **2013**<br>***RMB'000*** | 2012<br>*RMB'000* |
|---|---|---|---|
| Turnover | *2&3* | **30,383,420** | 28,987,545 |
| Cost of sales | | **(26,020,830)** | (25,058,481) |
| Gross profit | | **4,362,590** | 3,929,064 |
| Other revenue | *2&3* | **2,272,223** | 2,530,285 |
| Other income and gains | *4* | **662,770** | 695,563 |
| Selling and distribution expenses | | **(6,178,129)** | (5,886,383) |
| Administrative expenses | | **(737,080)** | (716,065) |
| Other operating expenses | | **(116,425)** | (39,602) |
| Share of profits of associates | | **85,896** | 153,967 |
| Finance costs | | **(144)** | (375) |
| Profit before tax | *5* | **351,701** | 666,454 |
| Income tax expenses | *6* | **(216,398)** | (214,302) |
| Total comprehensive income for the year | | **135,303** | 452,152 |
| Total comprehensive income attributable to: | | | |
| Owners of the Company | | **52,953** | 339,947 |
| Non-controlling interests | | **82,350** | 112,205 |
| | | **135,303** | 452,152 |
| Earnings per share – basic and diluted | *8* | **RMB0.05** | RMB0.30 |

**CONSOLIDATED STATEMENT OF FINANCIAL POSITION**
*AT 31 DECEMBER 2013*

| | NOTES | **31/12/2013** **RMB'000** | 31/12/2012 RMB'000 |
|---|---|---|---|
| Non-current assets | | | |
| Property, plant and equipment | | **3,080,898** | 3,309,928 |
| Construction in progress | | **319,073** | 254,650 |
| Land use rights | | **344,654** | 305,906 |
| Intangible assets | | **190,263** | 187,130 |
| Interests in associates | | **579,335** | 567,973 |
| Available-for-sale financial assets | | **250,986** | 36,358 |
| Held-to-maturity financial assets | | **–** | 239,622 |
| Term deposits | | | |
| – restricted | | **1,210,000** | 1,036,000 |
| – unrestricted | | **2,000,400** | 3,200,000 |
| Prepaid rental | | **120,983** | 106,451 |
| Deferred tax assets | | **203,369** | 200,951 |
| Other non-current assets | | **20,126** | 21,608 |
| | | **8,320,087** | 9,466,577 |
| Current assets | | | |
| Inventories | | **3,404,430** | 3,055,623 |
| Trade receivables | *9* | **76,682** | 113,707 |
| Deposits, prepayments and other receivables | | **1,030,083** | 1,180,816 |
| Amounts due from fellow subsidiaries | | **11,117** | 10,921 |
| Amounts due from associates | | **26** | 136 |
| Available-for-sale financial assets | | **258,474** | 641,252 |
| Held-to-maturity financial assets | | **240,980** | – |
| Financial assets at fair value through profit or loss | | **140,022** | – |
| Term deposits | | | |
| – restricted | | **1,271,365** | 3,345,000 |
| – unrestricted | | **890,000** | 401,000 |
| Cash and cash equivalents | | **4,877,493** | 2,589,154 |
| | | **12,200,672** | 11,337,609 |
| Total assets | | **20,520,759** | 20,804,186 |

*(Continued)*

| | NOTES | **31/12/2013** *RMB'000* | 31/12/2012 *RMB'000* |
|---|---|---|---|
| Capital and reserves | | | |
| Share capital | | **1,119,600** | 1,119,600 |
| Reserves | | **2,251,728** | 2,284,180 |
| Equity attributable to owners of the Company | | **3,371,328** | 3,403,780 |
| Non-controlling interests | | **277,292** | 364,900 |
| Total equity | | **3,648,620** | 3,768,680 |
| Non-current liability | | | |
| Deferred tax liabilities | | **88,398** | 84,619 |
| Current liabilities | | | |
| Trade payables | *10* | **4,542,397** | 4,295,654 |
| Other payables and accruals | | **2,110,854** | 2,213,756 |
| Coupon liabilities | | **9,930,631** | 10,259,260 |
| Deferred income | | **16,114** | 17,741 |
| Amounts due to fellow subsidiaries | | **44,169** | 35,802 |
| Amounts due to associates | | **16,571** | 8,904 |
| Bank borrowings | | **2,000** | 2,000 |
| Tax payable | | **121,005** | 117,770 |
| | | **16,783,741** | 16,950,887 |
| Total liabilities | | **16,872,139** | 17,035,506 |
| Total equity and liabilities | | **20,520,759** | 20,804,186 |
| Net current liabilities | | **(4,583,069)** | (5,613,278) |
| Total assets less current liabilities | | **3,737,018** | 3,853,299 |

## SELECTED NOTES TO THE CONSOLIDATED ACCOUNTS
*FOR THE YEAR ENDED 31 DECEMBER 2013*

### 1. PRINCIPAL ACTIVITIES

The Company is a public limited company incorporated in the PRC. The address of its registered office is Room 713, 7th Floor, No. 1258, Zhen Guang Road, Pu Tuo District, Shanghai, the PRC. The Company is listed on the main board of The Stock Exchange of Hong Kong Limited (the "Stock Exchange").

The directors of the Company consider that the Company's immediate holding company is Shanghai Friendship Group Incorporated Company, a company incorporated in the PRC and listed on the Shanghai Stock Exchange, and the Company's ultimate holding company is Bailian Group Co., Ltd (the "Bailian Group"), a state-owned enterprise established in the PRC.

The principal activities of the Company, together with its subsidiaries (the Company and its subsidiaries are collectively referred to as the "Group" thereafter) and its associates, are operation of chain stores including supermarkets, hypermarkets and convenience stores primarily in the eastern region of the PRC.

The consolidated financial statements are presented in Renminbi (the "RMB"), which is the same as the functional currency of the Company and its subsidiaries.

### 2. TURNOVER AND OTHER REVENUE

The Group is principally engaged in operation of chain stores including supermarkets, hypermarkets and convenience stores. Revenue recognised during the year is as follows:

| | **2013** | 2012 |
|---|---|---|
| | ***RMB'000*** | *RMB'000* |
| Turnover | | |
| Sales of merchandise | **30,383,420** | 28,987,545 |
| Other revenue | | |
| Income from suppliers | **1,614,687** | 1,936,934 |
| Gross rental income from leasing of shop premises | **585,075** | 517,913 |
| Royalty income from franchised stores | **58,681** | 57,506 |
| Commission income from coupon redemption in other retailers | **13,780** | 17,932 |
| | **2,272,223** | 2,530,285 |
| Total revenue | **32,655,643** | 31,517,830 |

### 3. SEGMENT INFORMATION

Information reported to the Group's general manager, who is the chief operating decision maker of the Group for the purposes of resource allocation and assessment of performance, is focused on three main operations of the Group identified in accordance with the business nature and the size of the operations.

The reportable operating segments of the Group are as follows:

- Hypermarket chain operation
- Supermarket chain operation
- Convenience store chain operation
- Other operations

There are no significant sales or other transactions between the segments. Other operations of the Group principally comprise sales of merchandise to wholesalers, provision of logistic services for wholesale business, and sales through internet. Other operations of the Group are aggregated when the information is reported to the Group's general manager.

The following is an analysis of the Group's revenue (including turnover and other revenue) and results by each reportable operating segment for the two years:

| | **Segment revenue** | | **Segment results** | |
|---|---|---|---|---|
| | **2013** | 2012 | **2013** | 2012 |
| | ***RMB'000*** | *RMB'000* | ***RMB'000*** | *RMB'000* |
| Hypermarkets | **19,665,632** | 18,883,020 | **98,557** | 233,788 |
| Supermarkets | **10,854,975** | 10,572,139 | **294,820** | 284,621 |
| Convenience stores | **2,052,961** | 1,963,173 | **(86,439)** | (24,123) |
| Other operations | **82,075** | 99,498 | **689** | 27,721 |
| | **32,655,643** | 31,517,830 | **307,627** | 522,007 |

A reconciliation of the total segment results to the consolidated profit before taxation is as follows:

| | **2013** | 2012 |
|---|---|---|
| | ***RMB'000*** | *RMB'000* |
| Segment results | **307,627** | 522,007 |
| Interest income | **57,848** | 63,980 |
| Unallocated income | **68,696** | 54,943 |
| Unallocated expenses | **(168,366)** | (128,443) |
| Share of profits of associates | **85,896** | 153,967 |
| Consolidated profit before taxation | **351,701** | 666,454 |

All of the segment revenue reported above is from external customers.

All of the Group's revenue and segment results is attributable to customers in the PRC.

Segment results did not include share of profits of associates, allocation of headquarter income and expenses (including certain interest income relating to funds centrally managed). This is the measure reported to the Group's general manager for the purposes of resource allocation and assessment of segment performance.

The following is an analysis of the Group's assets by operating segments:

| | **31/12/2013** | 31/12/2012 |
|---|---|---|
| | ***RMB'000*** | *RMB'000* |
| Segment assets | | |
| – Hypermarkets | **11,592,647** | 11,639,101 |
| – Supermarkets | **5,748,074** | 6,611,410 |
| – Convenience Stores | **710,582** | 531,960 |
| – Other operations | **151,823** | 371,930 |
| Total segment assets | **18,203,126** | 19,154,401 |
| Investments in associates | **579,335** | 567,973 |
| Other unallocated assets | **1,738,298** | 1,081,812 |
| Total assets | **20,520,759** | 20,804,186 |

Other unallocated assets principally comprise certain financial assets, cash and cash equivalents centrally managed by headquarter and deferred tax assets.

**Other segment information**

**2013**

| | **Hypermarkets** *RMB'000* | **Supermarkets** *RMB'000* | **Convenience stores** *RMB'000* | **Other operations** *RMB'000* | **Total** *RMB'000* |
|---|---|---|---|---|---|
| Amounts included in the measure of segment results or segment assets: | | | | | |
| Addition to non-current assets *(note)* | **228,168** | **176,476** | **65,175** | **212** | **470,031** |
| Depreciation | **318,155** | **144,672** | **39,464** | **14,539** | **516,830** |
| Amortisation | **3,306** | **6,957** | **814** | **5,755** | **16,832** |
| Impairment losses on property, plant and equipment | **39,592** | **3,240** | **394** | **–** | **43,226** |
| Loss on disposal of property, plant and equipment and intangible assets | **1,943** | **4,438** | **329** | **579** | **7,289** |
| Interest income | **272,066** | **73,947** | **9,351** | **65,457** | **420,821** |
| Finance costs | **–** | **–** | **–** | **144** | **144** |

**2012**

| | Hypermarkets *RMB'000* | Supermarkets *RMB'000* | Convenience stores *RMB'000* | Other operations *RMB'000* | Total *RMB'000* |
|---|---|---|---|---|---|
| Amounts included in the measure of segment results or segment assets: | | | | | |
| Addition to non-current assets *(note)* | 487,828 | 218,502 | 63,756 | 574 | 770,660 |
| Depreciation | 346,285 | 156,092 | 22,067 | 14,422 | 538,866 |
| Amortisation | 5,005 | 6,482 | 803 | 5,308 | 17,598 |
| Impairment losses on property, plant and equipment | 23,872 | 2,521 | 223 | – | 26,616 |
| Loss (gain) on disposal of property, plant and equipment | 830 | (765) | (63) | 115 | 117 |
| Interest income | 245,430 | 74,482 | 4,325 | 81,556 | 405,793 |
| Finance costs | – | – | – | 375 | 375 |

*note:* Addition to non-current assets include the additions of property, plant and equipment, construction in progress, land use rights, intangible assets and deposit for acquisition of property, plant and equipment.

### Geographical information

The Group's operations and non-current assets are substantially located in the PRC. Revenues from external customers are substantially derived from customers located in the PRC. Therefore, no analysis of geographical information is presented.

### Information about major customers

None of the revenue from any customer contributed over 10% of the total sales of the Group during the two years.

## 4. OTHER INCOME AND GAINS

| | **2013** | 2012 |
|---|---|---|
| | ***RMB'000*** | *RMB'000* |
| Interest income on bank balances and term deposits | **420,821** | 405,793 |
| Government subsidies *(note)* | **49,559** | 65,640 |
| Fair value change on financial assets at fair value through profit or loss | **12,673** | 3,938 |
| Interest income from available-for-sale financial assets | **31,443** | 52,709 |
| Interest income from held-to-maturity financial assets | **15,558** | 18,149 |
| Gain on disposal of associates | **8,963** | – |
| Dividend from unlisted equity investments | **377** | 10,011 |
| Salvage sales | **28,224** | 31,013 |
| Others | **95,152** | 108,310 |
| Total | **662,770** | 695,563 |

*note:* The Group received unconditional subsidies from PRC local government as an encouragement for the operation of certain subsidiary companies in certain areas.

## 5. PROFIT BEFORE TAXATION

| | **2013** | 2012 |
|---|---|---|
| | ***RMB'000*** | *RMB'000* |
| Profit before taxation has been arrived at after charging (crediting): | | |
| Amortisation and depreciation | | |
| Amortisation of other non-current assets | **1,482** | 1,523 |
| Amortisation of intangible assets | **9,793** | 10,808 |
| Amortisation of land use rights | **5,557** | 5,267 |
| Depreciation of property, plant and equipment | **516,830** | 538,866 |
| Total amortisation and depreciation | **533,662** | 556,464 |
| Share of profits of associates | | |
| Share of profit before taxation | **(114,607)** | (202,003) |
| Share of taxation | **28,711** | 48,036 |
| | **(85,896)** | (153,967) |

| | **2013** | 2012 |
|---|---|---|
| | ***RMB'000*** | *RMB'000* |
| Auditors' remuneration | **7,218** | 5,101 |
| Loss on disposal of property, plant and equipment and intangible assets | **7,289** | 117 |
| Impairment loss on property, plant and equipment recognised (included in other operating expenses) | **43,226** | 26,616 |
| Director's remuneration | **10,082** | 11,139 |
| Salaries, wages and other employee benefits of other staff | **2,623,918** | 2,415,765 |
| Retirement benefit scheme contribution of other staff | **276,084** | 258,661 |
| Total staff costs | **2,910,084** | 2,685,565 |
| Reversal of allowance for doubtful debts | **(3,836)** | (978) |
| Allowance for write-down of inventories | **21,239** | 2,328 |
| Cost of inventories recognised as expenses | **26,020,830** | 25,058,481 |

## 6. INCOME TAX EXPENSE

| | **2013** | 2012 |
|---|---|---|
| | ***RMB'000*** | *RMB'000* |
| Current tax on PRC Enterprise Income Tax ("EIT") | **215,037** | 235,682 |
| Deferred charge (credit) | **1,361** | (21,380) |
| | **216,398** | 214,302 |

No provision for Hong Kong Profits Tax has been made as the Group has no estimated assessable profits subject to Hong Kong Profits Tax.

Under the Law of the PRC on EIT and Implementation Regulation of the EIT Law, the EIT tax rate of the PRC subsidiaries is 25%. Certain subsidiaries are taxed at preferential rate of 15% as those entities which are located in specific provinces of western China and engaged in specific encouraged industries which enjoy a preferential tax rate of 15% under EIT Law. During the year, a group entity is qualified as "High Tech Enterprise" and enjoys a preferential tax rate of 15% under EIT Law and subject to renewal for every three years.

| | **2013** | 2012 |
|---|---|---|
| | ***RMB'000*** | *RMB'000* |
| Profit before tax | **351,701** | 666,454 |
| Tax at PRC EIT tax rate of 25% (2012: 25%) | **87,925** | 166,614 |
| Tax effect of share of profit of associates | **(21,474)** | (38,492) |
| Tax effect of expenses not deductible for tax purpose | **14,690** | 9,259 |
| Tax effect of income not taxable for tax purpose | **(2,560)** | (7,236) |
| Tax effect of tax losses not recognised | **154,586** | 154,946 |
| Utilisation of tax losses previously not recognised | **(14,934)** | (70,608) |
| Effect of preferential tax rates granted to certain PRC subsidiaries | **(1,835)** | (181) |
| Tax charge for the year | **216,398** | 214,302 |

## 7. DIVIDEND

| | **2013** | 2012 |
|---|---|---|
| | ***RMB'000*** | *RMB'000* |
| Dividend recognised as distribution during the year: | | |
| 2012 interim dividend RMB0.08 per share | **–** | 89,568 |
| 2012 final dividend RMB0.07 (2012: 2011 final dividend RMB0.12) per share | **78,372** | 134,352 |
| | **78,372** | 223,920 |

The directors do not recommend the payment of the final dividend (2012:RMB0.07 per share totalling RMB78,372,000) for the current year and is subject to approval by the shareholders of the Company in the upcoming annual general meeting.

## 8. EARNINGS PER SHARE

The calculation of the basic and diluted earnings per share is based on the following data:

| | **2013** | 2012 |
|---|---|---|
| | ***RMB'000*** | *RMB'000* |
| *Earnings* | | |
| Profit for the year attributable to owners of the Company | **52,953** | 339,947 |
| *Number of shares* | | |
| Weighted average number of ordinary shares for the purpose of basic and diluted earnings per share | **1,119,600,000** | 1,119,600,000 |

Diluted earnings per share are the same as basic earnings per share as no potential ordinary shares were outstanding during the two years.

## 9. TRADE RECEIVABLES

The aging analysis of the trade receivables net of allowance for doubtful debts at the end of the reporting period, arising principally from sales of merchandise to franchised stores and wholesalers with credit terms ranging from 30 to 60 days(2012:30 to 60 days), is as follows:

| **The Group** | **31/12/2013** | 31/12/2012 |
|---|---|---|
| | ***RMB'000*** | *RMB'000* |
| Within 30 days | **74,857** | 104,915 |
| 31-60 days | **860** | 5,922 |
| 61-90 days | **238** | 2,177 |
| 91 days – one year | **727** | 693 |
| | **76,682** | 113,707 |

Movement in allowance for doubtful debts is as follows:

| | **2013** | 2012 |
|---|---|---|
| | ***RMB'000*** | *RMB'000* |
| 1 January | **10,193** | 9,693 |
| Impairment losses recognised | **–** | 500 |
| Amounts reversed during the year | **(2,653)** | – |
| Amounts wrote-off during the year | **(5,849)** | – |
| 31 December | **1,691** | 10,193 |

## 10. TRADE PAYABLES

The aging analysis of trade payables at the end of the reporting period, arising mainly from purchase of merchandise with credit terms ranging from 30 to 60 days(2012:30 to 90 days), is as follows:

| **The Group** | **31/12/2013** | 31/12/2012 |
|---|---|---|
| | ***RMB'000*** | *RMB'000* |
| Within 30 days | **2,423,941** | 2,370,670 |
| 31-60 days | **866,503** | 822,974 |
| 61-90 days | **431,071** | 332,375 |
| 91 days – one year | **820,882** | 769,635 |
| | **4,542,397** | 4,295,654 |

## MANAGEMENT DISCUSSION AND ANALYSIS

### Operating Environment

The global and domestic economic environment in 2013 continued to be extremely complicated. On the international level, the global economy remained sluggish, global liquidity increased significantly, sovereign debt crisis repeatedly dampened the market confidence, and the profound impact of the financial crisis lingered. Domestically, growth in the consumer goods market slowed as the growth of economy continued to suffer from downward pressure. Due to the constant shifts in business structure, operational model and the overall outlook, China's chain retail industry continue to face intense competition and mounting challenges.

According to the National Bureau of Statistics, China's gross domestic product (GDP) increased by 7.7% year on year to RMB56.88 trillion in 2013, representing a steadily declined growth rate. Urban and rural resident income continued to grow relatively quickly, but at a slower pace year on year. Urban resident income per capita reached RMB29,547 with disposable income per capita rising to RMB26,955, an nominal increase of 9.7% year on year, and a real increase of 7% year on year when excluding the effect of price changes. The real growth rate was 2.6 percentage points lower than that of 2012. Per capita cash income of rural residents was RMB8,896, representing a nominal growth of 12.4% year on year and a real increase of 9.3% year on year when excluding the effect of price changes. The real growth rate was 1.4 percentage points lower than that of 2012.

China's 2013 consumer price index (CPI) remained at a stable and relatively low level, mainly due to the government's effective regulation. The producer price index (PPI), a leading indicator of CPI, however, has been declining since March 2012. These indicators demonstrated the sluggish growth of the domestic economy and the insufficient expansion of aggregate demand.

From an industrial perspective, China's retail industry has experienced two decades of rapid growth. In recent years, however, the traditional retail industry has reached an inflection point and entered into a low profit period as operational models have been negatively affected by the slowing down of macro economy growth, changing consumer habits and the rapid expansion of e-commerce. In particular, individual store customer traffic has also dispersed as a result of dense allocation of physical retail outlets. Additionally, strict restrictions on the spending of government and state-owned enterprises (SOEs) influenced overall market demand. In 2013, the total retail sales of social consumer goods were RMB23,438 billion, representing a year-on-year nominal growth of 13.1%, or a real growth of 11.5% year on year when excluding the effect of price changes. The growth rate decreased by 1.2 percentage points over that of 2012. According to the statistics from the China National Commercial Information Center (CNCIC), in 2013, the retail sales growth rate year on year of the 100 largest retail enterprises in China was 8.9%, which was 1.9 percentage points lower than that of 2012, representing a decline in two consecutive years, and had reached the lowest level since 2005. In particular, the sales growth of food and daily necessities significantly slowed down year on year. Food sales grew by 10.6% year on year, 3.5 percentage points lower than that of 2012. Sales of daily necessities grew by 6.7% year on year, 6.1 percentage points lower than that of 2012. The sales of 3,000 major nationwide retail enterprises monitored by the Ministry of Commerce of the People's Republic of China ("MOC") rose by 8.9% year on year, representing an increase of 0.6 percent point over that of 2012, whereas the sales from online shopping increased by 31.9% year on year, which means online sales was the key driver for growth. Sales from supermarket enterprises rose by only 8.3% year on year, which was 0.4 percentage point lower than that of 2012. In certain first and second-tier cities, the growth of chain supermarket industry even encountered a downward inflection point. In line with the statistics released by CNCIC, the total retail sales of the 100 largest retail enterprises of the week-long 2014 Chinese New Year Holiday (which ran from 30 January to 5 February 2014) decreased by 3.8% when compared to the week-long 2013 Chinese New Year Holiday (which ran from 9 February to 15 February 2013).

Under such unprecedented challenges, China's chain supermarket enterprises (including the Group) experienced increased operating pressure throughout 2013. Frequent and multi-dimensional competition narrowed the gains from merchandise in the industry, while sharp and rigid increase in various costs kept their overall profitability under pressure.

## Financial Review

### *Growth in turnover and consolidated income*

During the period under review, the Group recorded a turnover of RMB30.38 billion, representing a growth of 4.8% year on year. Same store sales increased by approximately 2.13%, representing an increase of 2.85 percentage points over that of 2012, benefiting mainly from optimization of product mix, effective promotion, the continuous transformation of outlets as well as maturing business circles surrounding the sub-new supermarket outlets that resulted in higher sales. However, the Group was aware of the enduring effects on retail industry from a slowdown in growth of macro-economy and government policies in terms of food safety and anti-corruption. In addition, the impact of the significant decrease of group consumption and the rapid development of e-commerce on physical chain supermarkets also intensified. As the chain supermarket industry faces an unprecedentedly tough market situation, the Group will proactively explore and innovate new marketing models in order to ensure its existing market share.

During the period under review, the Group recorded a gross profit of RMB4.36 billion, representing an increase of approximately 11.0% year on year, and the gross profit margin increased by 0.81 percentage point to approximately 14.36%. The main reasons for the increase are as follows: (i) the Group adjusted its marketing strategy and carried out a series of promotional activities to improve price perception to attract more customers and therefore increased turnover and gross profit; and (ii) the Group managed to lower its purchasing costs by solidifying its competitive edge of resource consolidation, as well as increasing sales rebates from suppliers through effective commercial negotiations.

During the period under review, consolidated income was approximately RMB7.30 billion, representing an increase of approximately 2.0% year on year, which was mainly attributable to the following factors: (i) the Group reduced the charges on suppliers and only remained sales rebates and three types of service fee to lower sourcing cost with enhanced transparency. During the period under review, merchandise gains increased by RMB0.10 billion over 2012 with the growth of sourcing volumes and turnover; and (ii) during the period under review, total rental income of the Group from the sublease of shop premises increased by approximately RMB0.07 billion over 2012 due to increased price of new and renewed sublease contracts. The consolidated income margin was 24.02%, representing a decrease of 0.66 percentage point over that of 2012. The Group's consolidated income did not achieve simultaneous growth with its turnover due to the Group's low price strategy in response to price competition in the industry and the impact of low prices in online shopping channels.

During the period under review, the Group maintained sufficient cash flow and ensured stable capital gains by prudent and professional management. However, with the rapid development of third-party payment cards as well as a dramatic decline in group demand, the growth in sales of the Group's single-purpose payment card showed a downward trend. Nevertheless, as the redemption of the payment cards increases, it will affect the growth in net operating cash inflow.

*Operating cost and net profit*

During the period under review, total distribution expenses and total administrative expenses of the Group amounted to RMB6,178,129 thousand and RMB737,080 thousand respectively, representing an increase of 5.0% and 2.9% year on year respectively. The overall cost ratio kept stable year on year. Major cost items such as labour, rent and utilities expenses increased rigidly to RMB2,910,084 thousand, RMB1,684,412 thousand and RMB560,627 thousand respectively. The main reasons are: (1) local governments across China raised minimum wage drastically during the period under review. In Shanghai in particular, minimum monthly wage increased to RMB1,620 from RMB1,450 in 2013, representing an increase of 11.7% year on year. The surge in minimum wage together with according surge in social insurance cost led to an increase in labour costs and the increment of labour cost accounted for 71.8% of the total cost increment for the period under review; and (2) since lease contracts of some outlets approached expiry, the rental price of renewed as well as new rental contracts increased drastically because of rising premises prices, leading to a year-on-year growth of rental cost. Facing escalating costs, the Group consolidated management resources from headquarters of the Group to maintain its cost management and control by optimizing employment structure and establishing cost control mechanisms in order to lower administrative expenses.

During the period under review, the Group recorded an operating profit of RMB265,805 thousand, representing a decrease of 48.1% year on year. Operating profit margin decreased by 0.90 percentage point to 0.87% year on year. The rising costs drove the operating profits of the Group decline drastically. During the period under review, the Group focused on fresh produce, carried out more promotions with enhanced membership system and pursued win-win situation by reducing charges items for contracted suppliers, hence boosting sales and gross profit and achieving an increase of merchandise gains by RMB0.10 billion. However, labor cost and rental cost recorded a rigid increase of RMB0.28 billion and brought down operating profit. The Group responded to the challenges of rising costs by innovating marketing models for more market share, establishing cost control mechanisms and seeking support for the government policies.

During the period under review, the Group's share of revenue of associated companies was RMB85,896 thousand, representing a decrease of 44.2% year on year. Affected by the sluggish market environment and policies, the turnover of associated companies of the Company grew slightly. In addition, the new outlets opened in recent years were still under incubation. At the same time, due to the increase in labour cost, rental cost and advertisement expenditure, their operating cost increased and profit decreased year on year. Shanghai Carhua Supermarket Company Limited ("Shanghai Carhua") opened four new outlets during the period under review. As at 31 December 2013, Shanghai Carhua had a total of 28 outlets.

During the period under review, the tax charge of the Group was RMB216,398 thousand. The Group paid close attention to fiscally supportive policies of the Chinese government and strove for financial support from various local governments to lower its tax rate. However, due to the gradual expiration of the tax holiday enjoyed by mature outlets and the requirement that each outlet be taxed independently, the Group was unable to balance its total profits across different regions, and thus its income tax rate increased substantially to 61.5%, resulting in a much bigger decrease rate of profit after tax than the decrease rate of profit before tax.

During the period under review, the Group recorded total profits of RMB351,701 thousand, representing a decrease of 47.2% year on year. Net profits attributable to shareholders of the Company amounted to RMB52,953 thousand, representing a decrease of 84.4% year on year. The net profit margin attributable to shareholders of the Company was 0.17%. Basic earnings per share were approximately RMB0.05 based on the issued share capital of the Company of 1,119.6 million shares.

***Cash flow***

During the period under review, the Group's net cash inflow was RMB2,288,339 thousand, mainly due to the decrease in term deposits. Cash and miscellaneous bank balances as at the period end was RMB10,249,258 thousand.

For the year ended 31 December 2013, the turnover period of the Group's trade payables was 59 days, and inventory turnover period was approximately 40 days.

During the period under review, the Group did not use any financial instruments for hedging purposes and the Group did not issue any hedging instruments as at 31 December 2013.

***Growth in retail businesses***

*Hypermarkets*

During the period under review, the turnover of the Group's hypermarket segment increased by approximately 5.7% year on year to RMB18,234,857 thousand, accounting for 60.0% of the Group's turnover, representing an increase of approximately 0.5 percentage point over that of 2012. Gross profit margin increased by 0.93 percentage point to 13.80%. Same store sales increased by approximately 1.22%. Consolidated income margin was approximately 23.63%, representing a decrease of 0.69 percentage point year on year. The segment operating profit was RMB98,557 thousand, representing a decrease of 57.8% year on year. The operating profit margin decreased by 0.81 percentage point year on year to 0.54% due to: (i) the rigid increase of labor cost by RMB166,848 thousand because of increase in minimum wage; and (ii) provision made for store closure so as to improve outlet quality. During the period under review, it is increasingly clear that the hypermarkets are facing considerable competitive pressure from specialty stores and shopping malls due to the slowdown in the growth of chain supermarkets business in China's first and second tier cities along with the lax implementation of the ban on commercial outlet construction in the past. The Group faced increasing competition from the continuous opening of new outlets in neighbouring areas by peer competitors. Although the Group has put greater effort on transformation in recent years, it's increasingly difficult to see the transformation through with short duration of leases and defects on some outlet properties. Facing challenging environment, the hypermarket segment leveraged its competitive advantages and adopted a "two-pronged driving" policy of building its image and enhancing its competitiveness. Firstly, the Group ensured the quality of its newly-opened outlets by strictly implementing its opening procedures, while putting greater effort into maintaining its sub-new outlets and deepening the transformation of its existing outlets, so as to enhance and consolidate its market share through establishing "key outlets". Secondly, in response to the growing trend of consumers conducting price comparisons facilitated by the release of price information on daily necessities sold in hypermarkets by the government, the Group continuously implemented marketing and promotional activities with the theme of "Beneficial Life" (惠生活). The Group attracted customers by promoting selected price sensitive daily necessities to boost demand and strengthening bulk sourcing of fresh produce (such as vegetables) to lower the price, and thereby increased demand for non price-sensitive merchandise. In addition, the effectiveness of the Group's marketing and promotional activities was enhanced with refined sales and marketing strategies, rational pricing strategies as well as enhanced profit margin analysis. Thirdly, the Group accelerated the functional adjustments of its outlets and highlighted the display of merchandise by arranging and dividing the outlets into certain specific areas such as "Baby/Child Area" and "Specialty Electrical Appliances Area" to cater to the customers' preferences and consumption habits. Meanwhile, the Group attached great importance to sublease area that can provide strong backup to its stores and enhance the customers' one-stop shopping, recreation and dinning experience in the hypermarkets.

| | **As of 31 December** | |
|---|---|---|
| | **2013** | 2012 |
| Gross profit margin *(%)* | **13.80** | 12.87 |
| Consolidated income margin *(%)* | **23.63** | 24.32 |
| Operating profit margin *(%)* | **0.54** | 1.35 |

*Supermarkets*

During the period under review, the turnover of the Group's supermarket segment increased by approximately 3.4 % year on year to RMB10,151,879 thousand, accounting for 33.4% of the Group's turnover. Same store sales increased by approximately 2.61%. Gross profit increased by approximately 6.9% year on year to RMB1,531,444 thousand, and gross profit margin increased by 0.49 percentage point year on year to 15.09%. Consolidated income margin of the supermarket segment was 23.28%, representing a decrease of 0.48 percentage point year on year. The segment operating profit was RMB294,820 thousand, and the operating profit margin was 2.90%, the same with that of previous year. During the period under review, consumers were willing to shop at nearby supermarkets given their respective constraints of unconvenience like lack of time or poor traffics, therefore, the supermarket segment increased in popularity among communities. However, since the customer traffic as hindered by the advent of e-commerce, wet markets and other wholesale markets, and the fact that many outlets of the Group with lease contracts approaching expiry have to be closed every year due to change of the commercial use of the properties by respective landlords or dramatically increased rentals, whereas the newly-opened supermarkets are not able to attain the equivalent sales as that of mature ones within a short period of time, the turnover of the segment grew slowly. Furthermore, the rising costs such as labor cost and rental cost continued to pose a great pressure to the profitability of supermarket segment. As such, the supermarket segment concentrated primarily on fresh produce operations, deepened outlet transformation, pushed ahead with the key outlet strategy, optimized product categories through enhancing core merchandises, established a price monitoring mechanism, enhanced the effects of joint sales, and consolidated its market share.

| | **As of 31 December** | |
|---|---|---|
| | **2013** | 2012 |
| Gross profit margin *(%)* | **15.09** | 14.60 |
| Consolidated income margin *(%)* | **23.28** | 23.76 |
| Operating profit margin *(%)* | **2.90** | 2.90 |

*Convenience stores*

During the period under review, the convenience store segment recorded a turnover of approximately RMB1,934,450 thousand, representing an increase of approximately 5.3% year on year, accounting for approximately 6.4% of the Group's turnover. Thanks to the improvement in the image of its convenience stores and promotion of its core merchandise over the past years, especially the growth of high-end "Quik" stores, the image of "Quik" brand has become increasingly popular among consumers and the average age of customers had lowered. During the period under review, the same store sales of convenience store segment grew faster than all other segments of the Group. In the Shanghai market, the convenience store segment outgrew all other retail businesses in the chain supermarket industry, indicating that its consumers have kept increasing with promising prospect. On the other hand, the challenges posed by foreign competitors and the rapid increase of various expenses all drove up the costs, which could not be covered by growth of sales and gross profit, thereby leading to lower profitability of such segment. Under such competitive circumstance, the segment accelerated the pace in optimizing its product mix, shortened the turnaround time of its new merchandise, further promoted instant food products, strived to realize the transformation of its existing outlets, explored new franchise model and increased value-added services by utilizing its network advantages. As a result, the same store sales of convenience store segment increased by approximately 11.13% during the period under review. Gross profit margin was 16.13%, representing an increase of 1.24 percentage points year on year. Consolidated income margin was 23.92%, representing an increase of 0.87 percentage point year on year. Despite the fact that there was good performance in same store sales growth, due to the rise in labor cost and rental cost by RMB46,730 thousand and RMB13,548 thousand respectively, operating loss of the segment was RMB86,439 thousand and operating profit margin dropped to -4.47%, both showing year-on-year decrease. The Group sped up the transformation and improvement of convenience stores and explored ways to increase the proportion of franchised convenience stores to reverse the downward trend of profitability.

| | **As of 31 December** | |
|---|---|---|
| | **2013** | 2012 |
| Gross profit margin (%) | **16.13** | 14.89 |
| Consolidated income margin (%) | **23.92** | 23.05 |
| Operating profit margin (%) | **-4.47** | -1.31 |

***Financial results analysis***

| | **For the twelve months ended 31 December** | | **Year-on-year change** |
|---|---|---|---|
| | **2013** | 2012 | |
| | ***RMB million*** | *RMB million* | *(%)* |
| Turnover | **30,383** | 28,988 | 4.8 |
| Gross profit | **4,363** | 3,929 | 11.0 |
| Consolidated income | **7,298** | 7,155 | 2.0 |
| Operating profit | **266** | 512 | -48.1 |
| Taxation | **216** | 214 | 0.9 |
| Profit attributable to shareholders of the Company for the period | **53** | 340 | -84.4 |
| Basic earnings per share *(RMB)* | **0.05** | 0.30 | -84.4 |
| Dividend per share *(RMB)* | **0** | 0.15 | – |

*Capital structure*

As at 31 December 2013, the Group's cash equivalents were mainly held in Renminbi, and the Group had no other bank borrowings, except for existing borrowings of RMB2,000,000 of a non-wholly-owned subsidiary of the Group.

During the period under review, equity attributable to shareholders of the Group decreased from RMB3,403,780 thousand to RMB3,371,328 thousand, which was mainly due to the profit for the period amounting to RMB52,953 thousand, dividends distribution amounting to RMB78,372 thousand, and acquisition of shares of subsidiaries amounting to RMB7,033 thousand.

*Details of the Group's pledged assets*

As at 31 December 2013, the Group did not pledge any assets.

*Exposure to foreign exchange risk*

Most of the income and expenditures of the Group are denominated in Renminbi. During the period under review, the Group did not experience any material difficulties or negative effects on its operations or liquidity as a result of fluctuation in currency exchange rates. The Group did not enter into any agreements or purchase any financial instruments to hedge its foreign exchange risks. The directors believe that the Group is able to meet its foreign exchange requirements.

*Share capital*

As at 31 December 2013, the issued share capital of the Company was as follows:

| **Class of shares** | **Number of shares in issue** | **Percentage** |
|---|---|---|
| Domestic shares | 639,977,400 | 57.16 |
| Unlisted foreign shares | 107,022,600 | 9.56 |
| H shares | 372,600,000 | 33.28 |
| Total | 1,119,600,000 | 100.00 |

*Contingent liabilities*

As at 31 December 2013, the Group did not have any material contingent liabilities.

**Operating Review**

*Outlet Development*

During the period under review, China saw a notable slowdown in its economic growth which negatively affected the development of the chain supermarket industry. Due to sluggish market demand and fiercer competition, the Group's newly-opened outlets require more time for incubation. Under such circumstance, the Group adhered to its strategic goal of "Becoming a Regional Leader and National Strong Player", steadily implemented its centralized development strategy, strictly followed the "Quality First" principle to reasonably formulate its outlet development plan, optimized the procedures for opening new outlets and closed down some underperforming outlets, thereby further improving the overall quality of its outlets.

During the period under review, three hypermarkets were opened in Hangzhou, Zhejiang Province, which helped consolidating the Group's market share in the area where it is in a dominant position. By identifying ideal locations, and taking early actions to begin the coordination and the preparation work for the opening of new outlets, the Group formulated the outlet opening procedures that are efficient and orderly to ensure the success of newly-opened stores. In addition, through careful research and inspection, the Group closed down several underperforming outlets and thereby strengthen its financial balancing capability under current economic conditions.

During the period under review, 153 new supermarkets were opened, including 21 directly-operated stores and 132 franchised stores. After taking into consideration high rental costs and the profitability of its newly opened outlets, the supermarket segment insisted on developing outlets in a scientific way, with a focus on both outlet opening and outlet renewal. For its new directly-operated outlets, the Group ensured the profitability of these stores by carefully studying the surrounding business environment, property conditions, and market positioning, etc.. For its franchised outlets, the Group further optimized the procedures for opening new stores, strictly implemented its outlet opening standards, and strengthened the unity of external signage design, interior decorations and management standards of its supermarkets, thus ensuring the reasonable operating scale and the sustainable development of its supermarkets.

During the period under review, 156 new convenience stores were opened, including 52 directly-operated and 104 franchised stores. During the period under review, the convenience store segment insisted on idea of broadening sources of income and reducing expenditures. To this end, the Group took initiatives to close down underperforming outlets without growth prospects and continued to promote the transformation of its existing outlets. A total of 160 stores were successfully transformed. The Group gradually optimized the market positioning, in-store environment and merchandise display of its outlets to improve their quality. The Group also explored new franchising models to improve the profitability of its franchised stores. Meanwhile, the Group accelerated the development of its high-end stores and innovated its operating and profitability models, so as to enhance its brand image among customers.

As at 31 December 2013, the Group had a total of 4,530 outlets, a decrease of 168 outlets from the end of 2012. The decrease was attributable to the closure of some franchised stores. The Group, as a state-owned enterprise, strictly observed relevant laws, regulations and its own rules in respect to food safety, outlet image and outlet management. Therefore, growth of the number of the Group's franchised stores did not meet expectations due to its focus on the profitability of newly-opened and renewed franchised outlets. Approximately 84% of the Group's outlets were located in Eastern China.

| | **Hypermarkets** | **Supermarkets** | **Convenience Stores** | **Total** |
|---|---|---|---|---|
| Direct operation | 156 | 641 | 929 | 1,726 |
| Franchised operation | – | 1,828 | 976 | 2,804 |
| Total | 156 | 2,469 | 1,905 | 4,530 |

*Note:* As at 31 December 2013.

***Strengthened Operational System***

During the period under review, facing huge pressure and challenges from the consumer goods market, the Group carefully monitored the changes in consumer demand and proactively strengthened its operational system. By promoting outlet transformation, the Group improved the management of its outlets, strengthened its price management, optimized its product mix and supplier structure and enhanced its operating capability.

Outlet transformation is an effective way to increase the intrinsic value of outlets and boost their sales. With rapid economic development, changing consumer demands and the perfection of laws and regulations, transformation in retail segments became inevitable. During the period under review, in order to enhance the competitiveness of its individual outlets and boost its sales, the Group pushed forward its outlet transformation by improving and expanding the services offered at its outlets. The Group focused on promoting outlet classification adjustment in respect to its hypermarket segment, constantly broadened functions of sublease area and offered more convenient services to improve its outlet image. The Group pushed ahead with its transformation by promoting a modularized product mix at its stores, implementing a differentiated pricing strategy, innovating its incentive and appraisal mechanism and improving community services in respect to its supermarket segment. The Group continued to implement the "lean but reinforced" strategy in respect to its convenience store segment, which involves improving store performance by reducing slow-moving merchandise and items to release shelf space while replenishing fast-moving merchandise, items and ancillary products in a timely manner, and fully promoted the perfected operation model to more stores. Meanwhile, the Group started to open high-end convenience stores and innovated its sales model, products mix and business philosophy. During the period under review, the Group opened 20 high-end convenience stores.

During the period under review, the Group improved the management of merchandise categories and product pricing by enhancing coordination between its operations and procurement teams. During the period under review, the Group conducted various promotions to probe into customers' preference in time and model of consumption. The Group also improved the overall sales of certain categories of merchandise through carrying out various customer-specific promotional activities, exerting its competitive edge on product quality and procurement and utilizing various media resources. During the period under review, the Group unified the sales of direct marketing (DM) merchandise and monitored the compensation for price differences through greater collaboration between the operation and procurement teams. This helped to integrate resources and increase sales and profitability, thus facilitating the transformation of the Group's profit model. Meanwhile, in addition to monitoring its gross profit on a daily basis, the Group also strictly maintained its overall profit margin by regularly streamlining and analyzing the gross profit of promotional merchandise. During the period under review, the Group perfected its outlets' market survey system and pricing adjustment process, fixed benchmark gross profit margins for product pricing, guided price adjustments and took initiatives to build a low-price brand image while maintaining its overall gross profit margin.

During the period under review, the Group proactively improved procurement techniques and optimized product mix to meet diversified customer demands and increase customer traffic and sales. The Group continued to procure quality merchandises from origins, further guaranteed product quality and price. As at 31 December 2013, the Group had 319 fresh produce supply bases and sales of produce from its own supply bases increased by 28% year on year. The Group constantly improved its procurement and distribution techniques for fresh produce, sold its merchandise at competitive prices, increased product categories, strengthened self-processing capability and voluntarily satisfied demands from its outlets, thus providing better conditions for outlet operation. The Group's vegetables self-procurement-and-sale model began to bear fruit with sales of fresh produce at the hypermarkets significantly increased over the previous year. In supermarket segment, the Group enlarged the supplier base of chilled seafood products to boost sales and tightened the monitoring of fruits and vegetables to lower spoilage and increase gross profit. In convenience store segment, the Group launched the fresh produce promotional campaign, and boosted the sale of core merchandise by improving fresh food operation. The Group made breakthroughs in its bento box sales, which demonstrated a positive momentum. During the period under review, the Group continued to expand the channels through which direct supply of merchandise could be sourced with a view to alleviate the pressure of decreasing margin. In addition, the Group secured the supply of scarce goods through investment in buyout. Through this strategy, the Group has improved its sales and at the same time realised a payoff of its buyout investment. During the period under review, the Group took opportunities to boost sales based on product features, introduced the "Lianhua-exclusive" merchandise and implemented multi-channel procurements, so as to ensure its competitive advantage in differentiated prices.

Private label merchandise have become an effective tool in the sluggish market and amid fierce competition in the global chain supermarket industry. During the period under review, the Group continued to enhance the development and marketing of its private label merchandise, and the sales of its private label merchandise saw a year-on-year increase of approximately 8.2%, accounting for 3.1% of the total sales. Promotion of "Little Q" branded merchandise in the convenience store segment has gradually shifted from manufactured products to foodstuffs, and from marketable merchandise and passive procurements to personalized merchandise and collections, and launched new merchandise in outlets across the country, thereby greatly enhancing the Group's brand image. During the period under review, the Group enhanced the procurement of imported products, improved its product classification system and optimized its sourcing channels, leading to a significant growth in the purchase of imported products.

During the period under review, the Group accelerated the construction of information systems and logistics system so as to further improve the management and operation of its business. By establishing and improving a unified corporate information management platform, the Group visualized its internal operation processes and enhanced communications between different business units, which promoted the optimization and adjustment of business processes to meet the demand. The Group improved its unified settlement system to cover its lease and sublease businesses, thus making its financial management more efficient and convenient. During the period under review, the Group constantly improved its financial and cash management system and built a direct link between banks and the Group, in order to provide detailed daily statistics on its cash position to improve its financial management and cash utilization. Meanwhile, the Group further improved its B2B management system to reinforce the management of various suppliers' licenses and the online publicity and verification of receipts and payments, and introduced an online new product launch channel to make supplier management more efficient. During the period under review, the Group built upon its existing logistics system to ensure the timely delivery of merchandise. The Group enhanced communications among its procurement teams, suppliers and outlets in respect of normal-temperature product distribution and raised the order fulfilment rate. The Group also explored the direct logistics model, and standardized its logistics model in collaboration with its procurement and operation teams. The separation of procurement and order of fresh produce clearly defined order responsibilities and improved inventory turnover and order fulfillment rate. Meanwhile, the Group established an information service station to manage the prominent demands of its outlets and improve outlet service quality. Jiangqiao logistics center is expected to start operation by the end of 2014 given to the undergoing main construction and supported works as well as the Group's careful operation plans. After acquiring land for the new logistics center in Yangxunqiao, Zhejiang Province in May 2013, the Group is in the preparation stage for project biddings.

During the period under review, the Group further tightened its food safety management to build a foundation of trust among customers. The Group constantly intensified its grip on outlet operations and standardized management process mainly by improving service quality, establishing standardized systems and conducting store inspections. The Group intensified the quality inspection and approval procedures for the sale of new merchandise and built the supplier site-visiting mechanism for quality assurance. The Group also formulated a product sampling plan to guarantee the quality of merchandise on shelves. When bird flu broke out in April 2013, the Group took responsive measures immediately to adjust and monitor its product mix, display resources, safety propaganda and marketing activities on a timely and orderly basis. The display area was adjusted less for poultry products and more for pork and beef products in a timely manner. As a result of the Group's vigorous promotions of beef, vegetables and seafood, the negative impact of the bird flu incident was minimized.

***Accelerated Reform and Innovation***

During the period under review, the Group adopted the contract negotiation model to transform its profit model in accordance with the principles from six ministries and commissions on charges by retailers on suppliers. The Group modified the items it charges suppliers when entering into the 2013 supplier contracts and removed all other charges apart from sales rebates and three types of service fee. These fees were used to promote the sales of suppliers' products, encouraging them to sell their products in large quantity and at cheaper prices. As a result, the Group transformed its procurement charging model and helped to build a stable and mutually beneficial retailer-supplier relationship. The Group believes that, although the transformation will have negative impact on its profitability in the short run, the adjustment in charges benefits modification of incentive system for suppliers as the transformation of profit model is rolled out across the whole chain supermarket industry. As a result, the sales of its merchandise will be expanded significantly, which is expected to promote a mutual cooperation between the Group and its suppliers.

During the period under review, the Group optimized its strategy of sublease area to attract more renowned brands to its outlets and improve the shopping experience of its customers, thus enhancing its profitability and brand image. Firstly, the Group proactively transformed model of sublease area and adjusted its strategy to attract merchants in accordance with changing market demands. To this end, the Group engaged quality merchants, introduced more renowned brand and chain merchants, raised the entry barriers for merchants and enriched the services of its outlets. Secondly, in order to offer more convenient services to residents around its outlets, the Group selected certain pilot outlets to establish a convenient service center to serve its customers and improve its brand image. Thirdly, the Group endeavoured to attract more merchants, introduced more prestigious brands and attempted to add luxury brands to its outlets while enhancing the management of merchants' licenses. For instance, in a 39,000-square-meter hypermarket opened by the Group in Hangzhou, Zhejiang Province, it introduced "Glora Citta" (歐凱城), a shopping area only for luxury brands such as GUCCI, PRADA, BURBERRY and other fashionable brands. This was added with the introduction of "Miaomi City" (妙喵城), an infant and children products area, and an infant bathing center, thus making breakthroughs in the one-stop shopping concept of hypermarkets.

During the period under review, the Group continued to roll out the "Beneficial Life" promotional campaign, for which over 250 daily necessities were sold at low prices to attract customers, and intensified and monitored product management in the "Beneficial Life" campaign. This involved unifying merchandise display and decoration rules, improving inventory management and analyzing sales, gross profit and cost consistency in a timely manner, and resulted in a continuous growth in sales of the merchandise selected for the campaign and traffics in stores. During the period under review, the Group constantly innovated marketing initiatives, enhanced promotional activities and launched a series of themed promotions to boost customer traffic, including a promotional campaign in a Wedding Expo exhibition and 25% discount for all non-food merchandise events. The Group also promoted seasonal merchandise to boost sales growth and identified other potentially marketable merchandise based on the constant monitoring of latest consumption trend, formulated a product display plan, offered more guidelines and recommendations to customers and helped outlets boost sales of seasonal products.

The Group's loyal consumers are its most valuable asset to combat challenges from e-commerce and physical competitors. During the period under review, the Group focused on carrying out member promotions, analyzing customer demand and improving member activities based on the upgraded membership system. During the period under review, the Group completed the development and improvement of various system functions and optimized the operational processes for its "Lianhua Mart", a one-stop shopping website (www.lhmart.com). Riding on these achievements, the Group constantly adjusted and replenished product categories on the website, and offered additional value-added services for its members. It also gradually increased its online members, and promoted online and offline interactions.

***Strengthened Cost Controls and Solidified Fundamental Management***

Judging from the macro-economic policies of the government, the rapid and rigid rise in labor and rental costs will continue to pose challenges. In reaction to this trend, the Group adopted a series of cost control measures to cope with the challenges caused by the general increase in costs during the period under review.

During the period under review, with a focus on "resource integration, channel optimization, management unification and cost-saving", the Group modified and adopted a flexible recruitment model to control labor costs within a reasonable range. The Group promoted the use of various forms of temporary employees in its outlets. To satisfy its workforce requirements, the Group took a series of designated initiatives such as optimization of shift work in outlets with professional personnel and granted incentives to internal staff for contracting certain work. The Group has not only integrated its recruitment channels regarding all segments to maximize the utilization of such channels and explored new models of cooperation, but has also implemented labour outsourcing. A pilot project called "Taking delivery on credit" was launched in several outlets of the Group to simplify internal hand-over procedures and manage employees working on night shifts more efficiently. Furthermore, the number of workers of nearby outlets on duty at night responsible for taking deliveries was decreased from two to one to increase efficiency and lower costs. Meanwhile, the Group also attempted to assign multi-functions to one position in stores to remove redundant positions in supermarkets, increase efficiency and provide motivations for employees, which has been proved effective.

During the period under review, the Group sought to increase internal potential and reduce costs and enhance efficiency through various expense controls and energy-saving measures. Firstly, the Group circulated expenses control targets and measures for 2013, which had positive results. Secondly, the Group improved its equipment supplier assessment system and optimized the tendering process for equipment procurement. As a result, the tendering and bidding process of the Group for equipment procurement has become more reasonable, and cost was reduced. Thirdly, the Group continued to adopt new energy-saving measures and equipments in some outlets. Meanwhile, the Group applied for subsidies as a result of its energy-saving efforts. Fourthly, following the guiding principle of "Using idle assets first", the Group made best and reasonable use of its idle assets so as to maximize their utilization rate, and therefore the expenditure on new equipments was reduced consequently.

**Employment, Training and Development**

As of 31 December 2013, the Group had a total of 56,187 employees, representing a decrease of 3,037 employees during the period under review. Total staff costs were RMB2,910,084 thousand.

During the period under review, in order to maintain staff stability and enhance the competitiveness of remuneration, the Group raised salary levels for all staff to ensure that the salaries of its staff, in particular, its frontline employees, were competitive. The Group further refined its performance assessment indicator system and appraisal and incentive plan, with a focus on assessing key areas and enhancing personalized appraisal, in an effort to improve the overall operating results and management level of the Group. For middle and senior management and professional personnel, the Group further aligned their compensation with business performance and implemented annual performance assessments. In addition, the Group intensified the efforts to make appraisals on its key talents and outstanding young management and reward them for their good performance on key projects with special bonuses and allowances for management trainees.

During the period under review, the Group further enhanced talent training, determined the training goals, training model and appraisal mechanism by revising the training plan for fresh graduates, young management trainees and middle-level management, and helped its management staff to improve their capabilities rapidly through career planning, special trainings, position rotation and special studies.

During the period under review, the Group developed a customized training program for all its staff across all levels, including its new or experienced staff at grassroots or high levels, and provided them with training courses on industrial situation, business expertises, management capabilities and work skills, in order to enable them to learn what they need to better develop their careers. In addition, as for the cultivation of skilled staff, the Group carried out several capability improvement trainings, work skills contests, the on-job apprentice training plan and other training plans during the period under review to adapt them to their posts rapidly.

**Strategy and Plan**

As shown in the blueprint of China's second round reform outlined by the Third Plenary Session of the 18th CPC Central Committee, the central government's general economic policy is to "sustain growth, re-adjust structure and promote reform". The moderately-expansionary fiscal policy and prudent monetary policy are expected to remain the same in the near future.

Government and corporate spending and shopping for gifts by courtesy have shrunk rapidly in recent years, new business models including e-commerce enjoy indisputable advantages over the physical retail networks in terms of policy and capital support, tax concessions, and industrial disciplines. In spite of the above, the chain supermarket industry expects to see continued development potential as the government rolls out market-oriented reforms and the market gradually balances out. In particular, China will continue to focus on expanding domestic demand to achieve a restructuring of the economy that will include increased urbanization along with constantly rapid growth in the working population's income. All these indicate a healthy Chinese economy that will maintain steady growth over a long period of time. As a result, the Group does not expect any material change in business environment for chain retail companies in 2014.

The majority of the Group's outlets are located in first and second-tier cities which are rapidly approaching market saturation, especially in city centers. The large number of its outlets and their respective business segments increases the pressure to restructure and the Group's migration from a decentralized merchandise management system to a centralized merchandise management system increases the risk the Group faces when adapting its operations and procurement processes. Therefore, it will adopt market-oriented measures in 2014 which shall focus on "deepening reform, enhancing transformation, solidifying foundation and developing steadily" and propel various work effectively with the enforcement of reform.

**Optimize business structure and persist in transformation and upgrade, which will be demonstrated by the development and transformation of outlets and the upgrade and optimization of merchandises management systems**. In 2014, in terms of development, the Group will focus on optimizing development structure by well preparing for new store openings, improving the quality of new stores and increasing market share through outlet expansion. In respect of existing outlets, the Group will speed up renovation of existing outlets by concentrating primarily on the key outlet strategy to upgrade internally. The Group will optimize its segments structure and classified outlets in each segment into store clusters or specific types of outlets based on their location and floor space. This will be done in order to pave the way for the establishment of guidelines to a modularized merchandise structure. To this end, the Group will increase the proportion of functioned merchandises in hypermarkets and intensify price management of similar merchandise to provide a one-stop shopping experience for the customers from the neighbourhood. Supermarkets focuses on segmentation, developing lifestyle galleries which are targeted at middle to high-end customers, fresh produce specialty stores for household consumers and ordinary supermarkets tailored for general consumers. Convenience stores will be further categorized into stores located in business districts, stores with high customer traffic and stores within communities in terms of their customers, merchandise and service.

With respect to development of franchise business, the Group will optimize the structure of its franchise business, strengthen the management and control of franchised stores through system reform and upgrade, explore a new profit sharing scheme and diversify the form of cooperation. The Group will increase its merchandise support to franchised stores and reinforce the operation of fresh produce in these stores, and will experimentally expand the operational scale of fresh produce in certain franchised stores. Self-procurement of vegetables will be introduced to franchised stores as soon as possible.

With respect to sourcing and procurement, the Group will continue to optimize its sourcing channels and improve procurement techniques to remove redundant procedures and lower sourcing cost. The Group will also take measures to boost its consolidated income by working with suppliers and encouraging suppliers to invest in marketing and sales. The Group will optimize its incentive and exit schemes for procurement staff who will be separated from merchandise management. This will encourage the transformation of procurement staff into sales personnel by providing an increased reward and elimination system for the procurement staff. To cope with conditions in the consumption market, the Group will optimize its product mix by strengthening category management, rationalizing price combination and promoting differentiation. This will aid the Group in establishing a solid price image and secure a stable profit margin.

As a result, the Group's capital expenditure is expected to amount to approximately RMB1.2 billion in 2014, with the focus on transformation of existing stores and on the supply chain system including IT and distributing infrastructure. For example, the Group plans to spend RMB300 million to RMB400 million on transformation of approximately 250 outlets, an addition of approximately RMB300 million on Jiangqiao Logistics Center, approximately RMB300 million on the first phase construction of Yang Xun Qiao project, which is a new logistics centre in Zhejiang Province as well as approximately RMB200 million on new stores. The capital expenditure structure of 2014 shows significant increase in investment in infrastructure and transformation when compared with that of past few years.

**Deepen reform and improve systems, which will be demonstrated by the enhancement and optimization of operational management procedures, information system and organizational structure**. In 2014, the Group will develop its regional management organizational structure based on the strategy as a regional leader. The Group's headquarters emphasize the unity of fundamental management, sharing of business resources as well as supervision and monitoring on frontline units. The Group will strive to reduce redundancy in overall organizational structure, streamline management, reduce management levels and improve efficiency of all business lines as well as speed up the response to market. The Group will focus on solving problems regarding product mix, pricing, display and sales so as to increase sales and customer traffic.

The Group will attach great importance to reinforce the research and optimization of business segments based on market-orientation, chain-orientation, professionalism and standardization, intensify market research, formulate business requirements in a scientific manner, refine management of store layout and optimize on-site management of outlets. Furthermore, the Group will continue to seek innovations in store cluster management, merchandise purchasing, pricing, displays as well as inventory management so as to optimize the existing systems and procedures. This will involve effects of overcoming the bottleneck of coordination between operation and procurement, strengthening the standardization of operation procedures and optimizing merchandise category management. The Group will intensify information sharing and communication among management units of the headquarters and between management units and outlets. The Group will establish an integrated operational system to optimize procurement, processing and distribution, and improve self-procurement and self-marketing of fresh produce capabilities so as to create a better price image and attract customers.

The Group will further improve its information system construction, strengthen the operation analysis by leveraging on the information platform to supervise and manage the development of various business segments. With respect to merchandise distribution, taking the commencement of operation of Jiangqiao logistics centre as a major breakthrough, the Group will formulate a scheme on centralized distribution of merchandises by the Group, optimize existing ordering procedures and increase the merchandise order fulfillment rate of outlets. Furthermore, the Group will determine and finalize the location of distribution centres in Jiangsu Province and Anhui Province to substantially raise centralized distribution to outlets, and on the above basis, speed up the application of delivery on credit, reverse logistics, distribution for e-commerce and social logistics services accordingly.

**Upgrade business philosophy and consolidate operational basis, which will be demonstrated by improvements in its capabilities in conducting key businesses**. In 2014, apart from strengthening sales and boosting customer traffic, the Group will work to enhance its management of consolidated income and get hold of the overall intrinsic relationships among sales, price, gross profit and income. The Group will also implement procedures to increase transparency and nurture a lean management system in order to improve its fundamental management level. Specific measures include promoting "fee-to-ratio" reform, setting out a detailed plan accordingly, promoting the transformation of profitability model, intensifying efforts to develop core merchandises and expanding operational capacity, introducing more new goods, attracting customers and promoting sales by selling fresh produce through integrated operation of procurement, process and distribution. Moreover, the Group will strengthen the support of physical outlets for the e-commerce platform and try to launch Online to Offline (O2O) pilot projects in some supermarket outlets. Innovation in marketing activities will also be encouraged, in particular, measures such as using modern media to attract young customers will be adopted. Furthermore, the Group will optimize its business model and expand the functions of sublease areas, so as to generate more income. Finally, the Group will optimize the organizational management system and procedures in its headquarters, streamline the functions of various departments, and raise their service awareness to support outlets and front-line work in a better way.

**Control costs and develop steadily with the focus of cutting cost through process re-engineering**. In 2014, the Group will continue to exert strict control on various costs in a scientific way, in order to enhance the Group's competitive edge. In particular, the Group will further capitalize on its advantage in centralized fund management to enhance the efficiency of fund, and further strengthen the awareness of cost control to strictly manage various fees and expenses. The Group will also improve its organizational system and proactively leverage on the advantage of scaled chains operation, so as to reasonably allocate resources, streamline work procedures and boost employee efficiency. The Group will further improve its employee incentive system, innovate new measures to promote its performance-oriented culture, and stimulate employees' enthusiasm towards work. Over the past few years, even though the Group had made some achievements in cost control, according to the basic requirements of chain operation management, there are still room for improvement in cost reduction regarding the optimization of organizational system, improvements in work procedures and application of advanced technologies.

Since 2012, both the market and the Group have progressed into a period for adjustment. Following two decades of development in chain supermarket industry, the government, society and enterprises at all levels have confronted difficult structural changes. The 18th National Congress of the Communist Party of China clearly specified the direction of reform to the chain supermarket industry, which is completely competitive. All problems, no matter relating to the structural adjustment of market demand or building up market order, will be solved gradually with the deepening of reform. The Group believes that a consensus has been reached as to how to improve operational capabilities and cultural development. Besides, the direction of fully recognizing the nature of chain supermarket business, enhancing efficiency through process re-engineering and capturing market advantage with economics of scale is what the Group shall stick to. The Group believes that forthcoming reform will help regaining growth momentum, allowing it to solidify its leading position in the market.

## Purchase, Sale or Redemption of Shares

From 27 June 2003, the date of listing of the Company's shares on The Stock Exchange of Hong Kong Limited (the "Stock Exchange"), to the date of this announcement, neither the Company nor any of its subsidiaries has purchased, sold or redeemed any of the listed securities of the Company.

## Final Dividend

The board of directors (the "Board") of the Company does not recommend the payment of final dividend for the year ended 31 December 2013.

## Audit Committee

The audit committee of the Company has reviewed the annual results of the Company for the year ended 31 December 2013 and confirmed that they are prepared in accordance with the applicable accounting standards, laws and regulations and appropriate disclosures have been made.

## Compliance with Model Code for Securities Transactions by Directors of Listed Issuers as set out in Appendix 10 of the Rules Governing the Listing of Securities on the Stock Exchange ("Listing Rules")

The Company has adopted the Model Code for Securities Transactions by Directors of Listed Issuers ("Model Code") as set out in Appendix 10 of the Listing Rules as code of conduct for securities transactions by all directors of the Company. After specific enquiries to the directors, the Board is pleased to confirm that all the directors have fully complied with the provisions under the Model Code during the period under review.

## Compliance with the Corporate Governance Code as set out in Appendix 14 of the Listing Rules

The Board is pleased to confirm that save and except for the matters as set out below, the Company has complied with all code provisions under the "Corporate Governance Code" (the "Code") under Appendix 14 of the Listing Rules during the period under review. Apart from the following deviation, none of the directors is aware of any information that would reasonably indicate that the Company is not or was not for any time of the period under review in compliance with the Code. Details of the deviation are set out as follows:

Provision A4.2 of the Code requires that every director (including those appointed for a specific term) shall be subject to retirement by rotation at least once every three years. The articles of association of the Company provides that each director shall be appointed at the general meeting of the Company and for a term of not more than 3 years, and eligible for re-election. Having taken into account the continuity of the implementation of the Company's operation and management policies, the articles of association contains no express provision for the mechanism of directors' retirement by rotation, thus deviating from the aforementioned provision of the Code.

For Provision A.6.7 of the Code:

Mr. Wong Tak Hung, non-executive director, and Mr. Lee Kwok Ming, Don, independent non-executive director, were unable to attend the eighth meeting of the fourth session of the Board convened on 25 March 2013 by the Company due to their work duties.

Mr. Ma Xin-sheng, then non-executive director, and Mr. Lee Kwok Ming, Don, independent non-executive director, were unable to attend the ninth meeting of the fourth session of the Board convened on 18 June 2013 by the Company due to their work duties.

Mr. Kazuyasu Misu, non-executive director, and Mr. Lin Yi-bin, then independent non-executive director, were unable to attend the tenth meeting of the fourth session of the Board convened on 21 August 2013 by the Company due to their work duties.

Ms. Cai Lan-ying, executive director, and Mr. Wang Zhi-gang, then non-executive director, Mr. Kazuyasu Misu and Mr. Wong Tak Hung, non-executive directors, were unable to attend the eleventh meeting of the fourth session of the Board convened on 31 October 2013 by the Company due to their work duties.

Ms. Xu Ling-ling, then executive director, Mr. Kazuyasu Misu and Mr. Wong Tak Hung, non-executive directors, and Mr. Lee Kwok Ming, Don, independent non-executive director, were unable to attend the extraordinary general meeting of the Company convened on 20 December 2013 due to their work duties.

Mr. Kazuyasu Misu and Mr. Wong Tak Hung, non-executive directors, and Mr. Lee Kwok Ming, Don, independent non-executive director, were unable to attend the twelfth meeting of the fourth session of the Board convened on 20 December 2013 by the Company due to their work duties.

After receiving the relevant materials for the Board meeting, they have authorized other directors of the Company to attend the meeting and vote on their behalf. The matters considered at the Board meetings were ordinary matters and all resolutions were passed smoothly. The Company had sent the related minutes to all members of the Board after the Board meeting so any director who was unable to attend the meeting was able to understand the resolutions passed at the meeting.

Moreover, the Company has provided the relevant materials relating to the extraordinary general meeting to all members of the Board before the meeting. All ordinary resolutions and special resolutions were passed smoothly at the extraordinary general meeting. The Company had sent the related minutes to all members of the Board after the extraordinary general meeting so any director who was unable to attend the meeting was able to understand the resolutions passed at the meeting.

For Provisions A.6.7 and E.1.2 of the Code, Mr. Ma Xin-sheng, then chairman of the Board and non-executive director, Mr. Wong Tak Hung, non-executive director, and Mr. Lee Kwok Ming, Don, the chairman of the audit committee and an independent non-executive director, were unable to attend the 2012 annual general meeting of the Company convened on 18 June 2013 due to their work duties. The Company has provided the relevant materials relating to the 2012 annual general meeting to all members of the Board before the meeting. All ordinary resolutions and special resolutions were passed smoothly at the annual general meeting. The Company had sent the related minutes to all members of the Board after the annual general meeting so any director who was unable to attend the meeting was able to understand the resolutions passed at the meeting.

## APPOINTMENT OF DEPUTY GENERAL MANAGER

The Board convened a meeting (the "Meeting") on 26 March 2014 and approved the appointment of Mr. Shi Hao-gang (Note) as a deputy general manager of the Company with effect from 26 March 2014.

By order of the Board
**Lianhua Supermarket Holdings Co., Ltd.**
**Chen Jian-jun**
*Chairman*

Shanghai, PRC, 26 March 2014

*As at the date of this announcement, the Board comprises:*

*Executive directors: Chen Jian-jun, Hua Guo-ping, Cai Lan-ying, Qi Yue-hong and Zhou Zhong-qi*

*Non-executive directors: Kazuyasu Misu and Wong Tak Hung*

*Independent non-executive directors: Xia Da-wei, Lee Kwok Ming, Don, Zhang Hui-ming and Huo Jia-zhen*

*Note:* Profile of Mr. Shi Hao-gang

Mr. Shi Haogang, aged 56, is a political work instructor. Mr. Shi graduated from Macao University of Science and Technology with a major in Business Administration in August 2001, and holds a postgraduate degree. From April 1976 to January 1979, Mr. Shi served as a platoon leader and the Youth League secretary of Nanhui Chaoyang Farm (南匯朝陽農場). From February 1979 to October 1995, Mr. Shi served as an officer of Shanghai Silk Weaving Factory No. 6 (上海絲織六廠). From November 1995 to May 2010, Mr. Shi worked in Hualian Supermarket Holdings Co., Ltd., where he had successively served as a key officer, deputy manager, and manager of human resources department, the assistant to the general manager and the general manager of Shanghai operations, the assistant to the general manager and the general manager of East China operations, the manager of the operation management department and the deputy general manager. From June 2010 to February 2012, Mr. Shi served as the deputy general manager of Shanghai Lianhua Supermarket Development Co., Ltd. Since March 2012, Mr. Shi has served as the general manager and deputy party secretary of Shanghai Lianhua Supermarket Development Co., Ltd.