特步國際控股有限公司

# Xtep International Holdings Limited

*(Incorporated in the Cayman Islands with limited liability)*

*Stock code : 1368*


*Sports like no other*

Interim Report 2008

Exceptional Feeling

# Contents

# Corporate Information

## Board of Directors

### Executive Directors

Ding Shui Po (丁水波) *(Chairman)*
Ding Mei Qing (丁美清)
Lin Zhang Li (林章利)
Ding Ming Zhong (丁明忠)
Ye Qi (葉齊)

### Non-executive Director

Xiao Feng (肖楓)

### Independent non-executive Directors

Sin Ka Man (冼家敏)
Xu Peng Xiang (許鵬翔)
Gao Xian Feng (高賢峰)

## Board Committees

### Audit committee

Sin Ka Man (冼家敏) *(Chairman)*
Xu Peng Xiang (許鵬翔)
Gao Xian Feng (高賢峰)

### Remuneration committee

Xu Peng Xiang (許鵬翔) *(Chairman)*
Gao Xian Feng (高賢峰)
Ding Mei Qing (丁美清)

### Nomination committee

Ding Shui Po (丁水波) *(Chairman)*
Xu Peng Xiang (許鵬翔)
Gao Xian Feng (高賢峰)

## Company Secretary and Qualified Accountant

Ho Yui Pok, Eleutherius (何睿博) ACA, CPA

## Authorised Representatives

Ding Shui Po (丁水波)
Ho Yui Pok, Eleutherius (何睿博)

## Registered Office

Cricket Square
Hutchins Drive
P.O. Box 2681
Grand Cayman KY1-1111
Cayman Islands

## Head Office in The PRC

Economic and Technical Development Zone
Quanzhou City
Fujian Province
PRC 362000

## Principal Place of Business in Hong Kong

Suite 2401-2
24/F, Shui On Centre
6-8 Harbour Road
Wanchai, Hong Kong

## Legal Adviser as to Hong Kong Laws

Coudert Brothers in association with
Orrick, Herrington & Sutcliffe LLP

## Auditors

Ernst & Young

## Compliance Adviser

Shenyin Wanguo Capital (H.K.) Limited

## Cayman Islands Principal Share Registrar and Transfer Office

Butterfield Fund Services (Cayman) Limited
Butterfield House
68 Fort Street
P.O. Box 705
Grand Cayman KY1-1107
Cayman Islands

## Hong Kong Branch Share Registrar and Transfer Office

Computershare Hong Kong Investor Services Limited
Shops 1712-1716, 17th Floor
Hopewell Centre
183 Queen's Road East
Wanchai, Hong Kong

## Principal Bankers

China Construction Bank
(Quanzhou Qingmeng Sub-branch)
Agricultural Bank of China
(Quanzhou Economic and Technical Development Zone Sub-branch)
China Merchants Bank
(Quanzhou Quanxiu Sub-branch)
Industrial Bank Co., Ltd.
(Jinjiang Chen Geng Sub-branch)
Bank of Communications
(Quanzhou Branch)
Industrial Bank Co., Ltd.
(Xiamen Branch)
Hang Seng Bank Limited
China Construction Bank
(Hong Kong Branch)

## Investor Relations Consultant

Porda International (Finance) P.R. Group

## Company Website

www.xtep.com.hk

# Financial Highlights

> Successfully listed on the main board of the Hong Kong Stock Exchange on 3 June 2008

> 1H2008 revenue and profit results exceeded the full year of 2007

> Revenue rose by 174.3% to RMB1,408,197,000

> Gross profit margin increased by 4.6 percentage points to 36.8%

> Net profit increased by 214.1% to RMB254,664,000

> Average sales per retail outlet of Xtep brand increased by 45.4%

> Basic earnings per Share rose by 190.0% to RMB16.01 cents

> Interim dividend of HK5.0 cents (RMB4.4 cents) per Share, representing 38% of 2008 interim profit

## Cautionary Statement Regarding Forward-looking Statements

This Interim Report 2008 contains certain forward-looking statements with respect to the financial condition, results of operations and business of the Company. These forward-looking statements represent the Company's expectations or beliefs concerning future events and involve known and unknown risks and uncertainty that could cause actual results, performance or events to differ materially from those expressed or implied in such statements. Certain statements, that include wordings like "potential", "estimated", "expects", "anticipates", "objective", "intends", "plans", "believes", "estimates", and similar expressions or variations on such expressions may be considered "forward-looking statements". Forward-looking statements involve inherent risks and uncertainties. Readers should be cautioned that a number of factors could cause actual results to differ in some instances materially, from those anticipated or implied in any forward-looking statement. Forward-looking statements speak only as of the date they are made, and it should not be assumed that they have been reviewed or updated in the light of new information or future events. Trends and factors that are expected to affect the Company's results of operations are described in the sections of "Business Review" and "Financial Review".

| Six months ended 30 June | 2008 | 2007 | Changes |
|---|---|---|---|
| | RMB million | RMB million | |
| **Profitability data** | | | |
| Revenue | 1,408.2 | 513.4 | +174.3% |
| Gross profit | 517.8 | 165.0 | +213.7% |
| Operating profit | 300.8 | 96.5 | +211.8% |
| Profit for the period | 254.7 | 81.1 | +214.1% |
| Basic earnings per Share (RMB cents) (Note 1) | 16.01 | 5.52 | +190.0% |
| **Profitability ratios** | (in %) | (in %) | (in % pt) |
| Gross profit margin | 36.8 | 32.2 | +4.6 |
| Operating profit margin | 21.4 | 18.8 | +2.6 |
| Net profit margin | 18.1 | 15.8 | +2.3 |
| Effective tax rate | 14.2 | 11.3 | +2.9 |
| Return on average total equity holders' equity (Note 2) | 17.7 | 33.0 | |
| **Operating ratios** (as a percentage of revenue) | (in %) | (in %) | (in % pt) |
| Advertising and marketing expenses | 8.0 | 5.6 | +2.4 |
| Staff costs | 5.3 | 10.0 | (4.7) |
| Research and development | 1.6 | 1.3 | +0.3 |

| | As at 30 June 2008 | As at 31 December 2007 |
|---|---|---|
| **Asset and Working Capital ratios** | | |
| Current asset ratios | 4.4 | 1.9 |
| Gearing ratios (Note 3) | 9.4% | 41.5% |
| Net asset value per Share (RMB cents) (Note 4) | 118.1 | N/A |
| Average inventory turnover days (Note 5) | 58 * | 68 ** |
| Average trade receivables turnover days (Note 6) | 47 * | 56 ** |
| Average trade and bills payables turnover days (Note 7) | 43 * | 30 ** |

Notes:

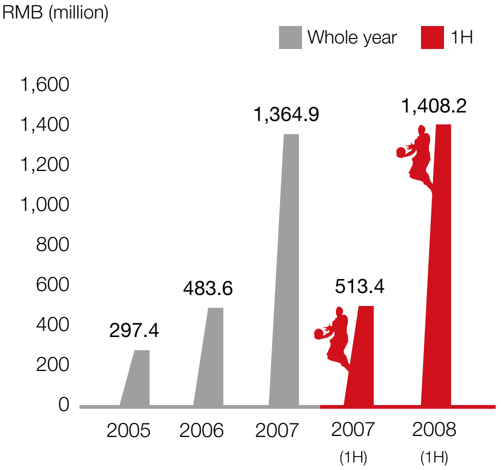
1) The calculation of basic earnings per Share is based on the profit attributable to equity Shareholders of the Company divided by the weighted average number of ordinary shares in issue during the relevant period.
2) Return on average total equity holders' equity is equal to the profit for the period divided by the average opening and closing total equity holders' equity
3) The calculation of gearing ratio is based on the total borrowings divided by the sum of share capital and reserves of the Company at the end of the period.
4) The calculation of net asset value per Share is based on the total number of shares in issue after the Listing and at the end of the period.
5) Average inventory turnover days is equal to the average opening and closing inventory divided by costs of sales and multiplied by number of days in the relevant period.
6) Average trade receivables turnover days is equal to the average opening and closing trade receivables divided by revenue and multiplied by number of days in the relevant period.
7) Average trade and bills payables turnover days is equal to the average opening and closing trade and bills payables divided by cost of sales and multiplied by number of days in the relevant period.

* In 183 days

** In 365 days

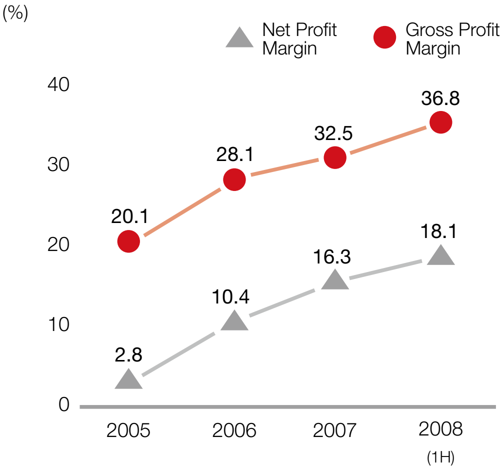
## Revenue

RMB (million)



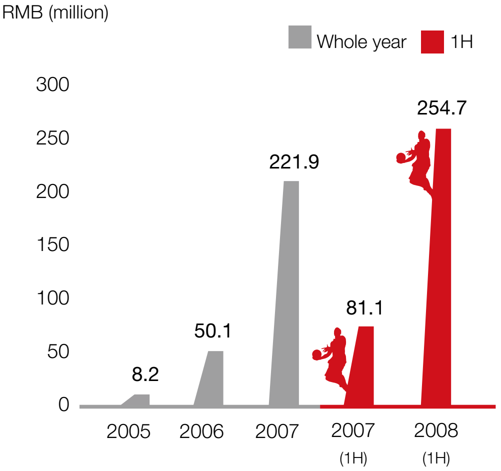

## Margins

(%)



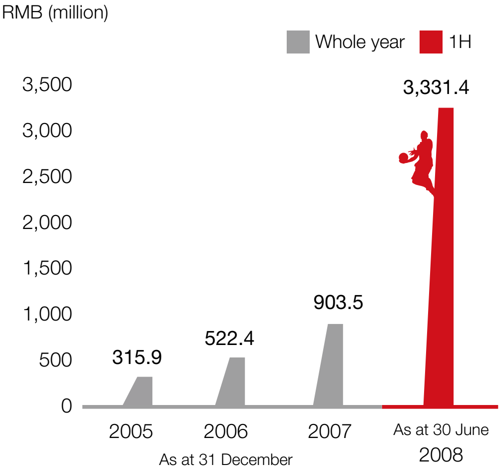

## Profit for the year

RMB (million)



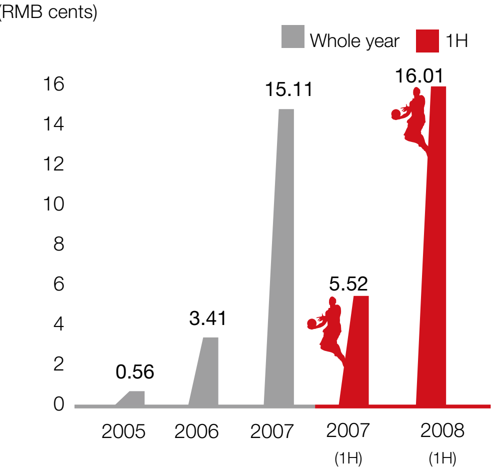

## Total assets

RMB (million)



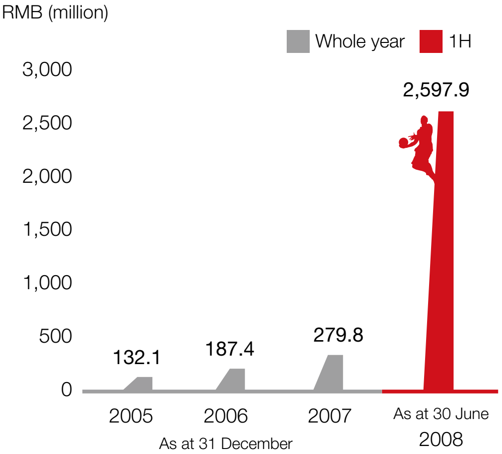

## Basic earnings per Share

(RMB cents)




## Total equity

RMB (million)

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# Chairman's Statement

**Ding Shui Po**
*Chairman*

Dear Shareholders,

On behalf of the Board, I am pleased to present the first interim report of the Company for the six months ended 30 June 2008 following its successful Listing on the main board of the Hong Kong Stock Exchange on 3 June 2008. To capture market opportunities, the Group places strong emphasis on brand building, actively marketing its brand recognition and desirability, as well as enhancing its own research and development capabilities and building a more extensive distribution network. The Group had therefore been able to meet its planned operational and financial objectives in the first half of 2008, laying a solid foundation for the future.

With continuous expansion in operations and an increase in operational efficiency, the Group recorded strong sales revenue growth and encouraging overall profitability for the first half of 2008. During the period under review, the Group's revenue amounted to RMB1,408.2 million, an increase of 1.7 times as compared to the same period last year (2007: RMB513.4 million). Profit attributable to Shareholders grew by 2.1 times over the same period last year to RMB254.7 million (2007: RMB81.1 million). Basic earnings per Share was RMB16.01 cents, an increase of 1.9 times as compared to the same period last year (2007: RMB5.52 cents). As operating

and financial conditions have improved significantly, the Board has proposed to declare an interim dividend of HK5.0 cents (RMB4.4 cents) per Share, representing approximately 38% of the net profit available for distribution to our Shareholders. This pay out ratio is also representing the fulfillment of our promise stated in the Prospectus of the Company that the Group intended to declare dividends of no less than 30% of the Group's net profit.

The year 2008 represents an important milestone in the history of the Group and at the same time it is a flourishing year for China to host the Beijing 2008 Olympic Games. The Listing was well-received by global investors with net proceeds from the global offering amounting to approximately HK$2.1 billion, establishing a sound foundation for future development. In addition, the Group has Carlyle's investment funds invested as Shareholders of the Company. Not only does this reflect Carlyle's investment funds' confidence in China's sportswear market and the future of the Group, but our relationship with this investor also adds strategic value to the Group and further strengthens the Company's corporate governance structure.

I believe that the successful Listing of the Company merely marks the beginning investment of its real development. As the Chinese economy continues to grow rapidly, the purchasing power and living standards of the general public in China will increase, creating huge potential for the sportswear market in China. According to Euromonitor International, the total size of China's sportswear market is expected to increase to approximately RMB131.2 billion in 2012, representing a CAGR of approximately 26.0% from 2006 to 2012. In order to seize this opportunity in a timely manner, the Group has focused its efforts on increasing the market penetration of the Xtep, Disney Sport and Koling brands in high growth regions in China, as well as increasing its spending on brand-building and research and development. As a result, the Group achieved satisfactory financial performance for the period under review with revenue for the first half of 2008 exceeding that for the full year of 2007. The Beijing 2008 Olympic Games have boosted the PRC public's interest in sports. We believe that sports will continue to increase in popularity in the Asia-Pacific region as more major international sports competitions will be held in the region in the future, bringing brighter prospects for China's sportswear market. The Group was successfully appointed as the sole sports product partner for the 11th National Games of China, which will be held in Jinan City, Shandong in October 2009 and is the largest national sports event organized by the National Sports Committee in the PRC. We believe that the recognition of the Xtep brand will be further enhanced through such sporting event.

The Group places great importance on supporting and working with the communities in which it operates and takes social responsibilities seriously. In respond to the snowstorm in China in February 2008 and earthquake in Sichuan in May 2008, the Group immediately made cash and goods donations, as well as rallying its staff and business parties to support and participate in such donations.

Our vision is to become one of the top international leaders in the fashion sportswear market. Looking ahead, in order to realize Xtep's focus on fashionable experience and its brand ideology of bringing relaxation pleasure to sports, the Group will optimize its distribution network and establish brand new flagship stores to further enhance and crystalize its brand image through innovative designs and spacious retail outlets. Customers will be introduced to a new and improved shopping experience in an effort to further drive up the Group's profit.

In addition, Xtep will continue to adhere to its effective, innovative and multi-faceted marketing strategies that combine sports marketing and entertainment marketing, and offer strong support and training services to its distributors in order to increase customer loyalty through premium quality customer service. Product design and research and development are crucial to the success of the Group and hence we will increase the cooperation with worldwide international consultants to continue our unique brand essence. Looking ahead, Xtep will strengthen its efforts in these areas to sustain our continuous growth so as to gradually advance towards a more prosperous future.

In a market environment surrounded with both opportunities and challenges, the Group's most valuable asset is its innovative and diligent staff. On behalf of the Board, I would like to take this opportunity to express our sincere gratitude to our staff for their dedication and contributions to the Group, and also to our Shareholders and business partners for their strong support and trust over the years. The Group will continue to strengthen its competitive edge and to strive for excellent results to reward our Shareholders for their continuous support.

**Ding Shui Po**
*Chairman*

Hong Kong, 1 September 2008


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# Management Discussion and Analysis


## Business Overview

Xtep is the leading domestic fashion sportswear enterprise in the PRC. Listed on the main board of the Hong Kong Stock Exchange on 3 June 2008, the Group is principally engaged in the design, development, manufacture and marketing of sportswear, including footwear, apparel and accessory products, sold under the Xtep brand and the Koling brand, which are owned by us and the Disney Sport brand, which is licensed to us in the PRC. According to Euromonitor International, Xtep brand is the largest domestic fashion sportswear brand in terms of revenue for 2007.

## Market Review

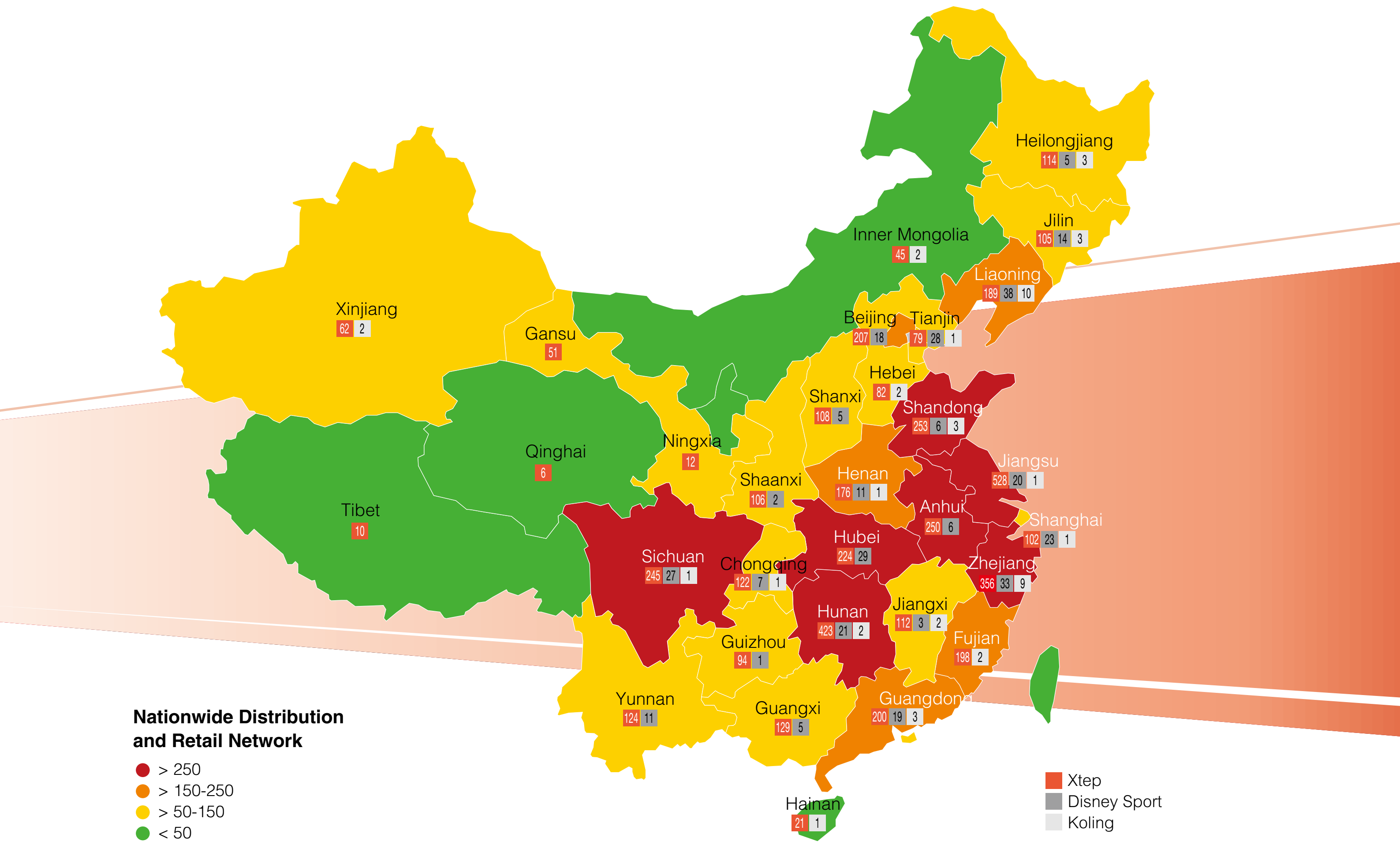
The strong economic performance of the PRC and increasing affluence of its citizens have contributed to the country's increased purchasing power. With the growing middle class and the increasing affluence of the country, the consumer goods market in the PRC is rapidly expanding. The sportswear industry in the PRC is driven by the economic growth of the country, particularly the increasing disposable income of its citizens. In general, there is still huge development potentials in the sportswear industry in the PRC. According to Euromonitor International, it is expected that the total size of the sportswear market in the PRC will grow at a CAGR of 26% from RMB32.8 billion in 2006 and reach approximately RMB131.2 billion by 2012. In addition, the Beijing 2008 Olympic Games and the 11th National Games of China in 2009 will also drive the growth of the overall sportswear industry in the PRC. The Group believes that such growth could be sustained.

## Business Review

### Distribution management and retail network expansion

As the leading domestic fashion sportswear enterprise in the PRC, the Group actively seizes opportunities in developing its distribution network in the high-growth regions in China. For the six months ended 30 June 2008, the retail network of the Xtep, Disney Sport and Koling brands operated by our distributors and third-party retailers covered 31 provinces, autonomous regions and municipalities in China. The following table sets out the number of retail outlets operated by our distributors and third-party retailers in the PRC under Xtep, Disney Sport, and Koling brands as at 30 June 2008:

| Number of retail outlets | | | | |
|---|---|---|---|---|
| Brands | As at 31 December 2007 | Addition | Consolidated | As at 30 June 2008 |
| Xtep brand | 4,380 | 398 | (45) | 4,733 |
| Disney Sport brand | 217 | 121 | (6) | 332 |
| Koling brand | 50 | – | – | 50 |
| Total | 4,647 | 519 | (51) | 5,115 |




The following table sets out the number of retail outlets operated by our distributors and third-party retailers in the PRC under the Xtep, Disney Sport and Koling brands as at 30 June 2008 by geographical region:

| Number of retail outlets | | | | | | |
|---|---|---|---|---|---|---|
| | Xtep brand | | Disney Sport brand | | Koling brand | |
| Regions | Number of retail outlets | % | Number of retail outlets | % | Number of retail outlets | % |
| Eastern region | 1,799 | 38 | 91 | 27 | 18 | 36 |
| Southern region | 1,173 | 25 | 85 | 26 | 7 | 14 |
| Western region | 832 | 18 | 48 | 14 | 4 | 8 |
| Northern region | 929 | 19 | 108 | 33 | 21 | 42 |
| Total | 4,733 | 100 | 332 | 100 | 50 | 100 |

Note:

Eastern region includes: Jiangsu, Zhejiang, Anhui, Shandong, Fujian, Jiangxi and Shanghai

Southern region includes: Hunan, Hubei, Guangdong, Henan, Guangxi and Hainan

Western region includes: Sichuan, Yunnan, Chongqing, Shaanxi, Guizhou, Xinjiang, Gansu, Ningxia, Tibet and Qinghai

Northern region includes: Beijing, Liaoning, Heilongjiang, Shanxi, Jilin, Hebei, Tianjin and Inner Mongolia

In addition, the Group also operates and manages retail outlets where it sells Xtep and Disney Sport products directly to consumers. As at 30 June 2008, the Group has one self-managed retail outlet for Xtep branded products and one self-managed retail outlet for Disney Sport branded products, both of which are located adjacent to the Group's headquarters in Quanzhou, Fujian province. These retail outlets primarily serve the purposes of facilitating research and experimentation with various store designs and layouts, as well as allowing us to conduct consumer preference tests.



## Management and training

As the Group distributes its products through its extensive nationwide network, Xtep has formulated a stringent distributor management system. Apart from conducting random inspections of retail outlets regularly, the Group also provides training for its distributors and staff working at the retail outlets. For the six months ended 30 June 2008, the Group has organized numerous trainings in, for example, Guangzhou, Wenzhou, Changsha, Anhui, Chongqing, Beijing, Guiyang and Shanxi, with approximately 800 attendees. Moreover, the Group implemented a distribution resource planning ("DRP") system in 2007, which links up the production, inventory and financial systems, allowing it to track inventory levels and the movement of its products at the warehouses and certain retail outlets operated by the Group, its distributors and third-party retailers. For the six months ended 30 June 2008, the retail outlets adopting the DRP system accounted for approximately 25% of the total number of retail outlets.

## Sales fair

Since 2007, we have organised four seasonal sales fairs every year for each of our brands. During the first half of 2008, the Group organized two of these seasonal sales fairs, namely Autumn Sales Fair 2008 held in Beijing in February and March 2008 and the Winter Sales Fair 2008 held in Fujian in May 2008. More than 3,000 representatives from our distributors and third-party retailers participated in each of these two seasonal sales fairs, where the orders placed by our distributors reached historical highs.

## Brand building and marketing

The Group is one of the first sportswear enterprises in China to position its own branded sportswear products with a focus on fashion and trends, in addition to functionality and utility. During the period under review, the Group continued to pursue its marketing and promotion strategies, which combine sports marketing and entertainment marketing, and implemented various innovative and comprehensive marketing activities, including promotion by entertainment celebrities, sponsorships of national sporting and entertainment events, various forms of advertising, retail sales promotions and other promotional activities.


The Group's major marketing and promotional activities for the six months ended 30 June 2008 are as follows:

## Promotion by entertainment celebrities

The Group is one of the first in its industry in China to deploy a marketing campaign using entertainment celebrities to promote brands and products that attract and appeal to fashion-conscious consumers. During the period under review, the Group selected such entertainment celebrities as Nicholas Tse, Jolin Tsai, Wilber Pan, and Twins as image and brand representatives of the Xtep brand. The Group believes that this marketing strategy has been effective in attracting its target consumers to the Xtep brand, which has resulted in the increased market awareness and acceptance of the Xtep brand as a trend-setting sportswear brand. The Group also takes advantage of concerts, new CD release promotional activities and autograph sessions organised by its brand and image representatives to promote the brands and products of the Group. During the period under review, some of the promotional activities attended by Xtep's image and brand representatives include: the 22nd China Sports Show, canvass session of the 6th Southeast Music Chart Awards, and the Autumn Sales Fair 2008.

## Sponsorships of sports teams and events

The Group strategically sponsors selected national and college sports leagues and sports events to increase the Xtep brand's exposure in different levels nationwide.

The Group's sports-related sponsorships for the six months ended 30 June 2008 include:

- Sole title sponsor of the Women's Chinese Basketball Association (WCBA) 07-08;
- Sole title sponsor of the National Basketball League (NBL);
- Sponsor of "Xtep Cup" of the Yangzhou Jianzhen International Marathon;
- Sole title sponsor of the CX-Games organised by the Chinese X Games Association;
- Sportswear sponsor of "Amway Nutrilite Healthy Run" in 21 cities in China;
- Jiangsu Youth Sunshine Sports Competition; and
- Zhejiang Secondary Student Basketball League.



## Olympics marketing

The Beijing 2008 Olympic Games has been under the global spotlight. During this period, the Group has taken this opportunity to launch numerous Olympics-related marketing activities to seize the opportunity to introduce the Xtep brand to the media and the general public all over the world so as to enhance the brand awareness in the international arena. We were, among others:

- Designer and provider of footwear, apparel and accessory products to the Belarusian Olympic delegation, which were worn at awards ceremonies and other ceremonial and social events, as well as press conferences and celebration dinners at the Beijing 2008 Olympic Games;
- Sole sponsor of Xtep Olympic Train, which has been decorated with various Xtep logos, trademarks and images in relation to the Beijing 2008 Olympic Games, in order to enhance Xtep's brand position through the popularity of the Olympics; and
- Sole PRC sportswear enterprise that has successfully secured television commercial airtime during all finals of the Beijing 2008 Olympic Games on the CCTV Sports Channel, which is the official television channel in the PRC authorized to broadcast the Beijing 2008 Olympic Games.

We believe the above sponsorships and effective television commercial airtime during the finals of the Beijing 2008 Olympic Games have attracted thousands and millions of audience's attention about Xtep brand.

## Media advertising

During the period under review, the Group invested tremendous resources in media advertisements and other different promotion channels for brand marketing, so as to increase the domestic exposure of its three brands

- Invited the Group's image and brand representatives, namely Nicholas Tse, Jolin Tsai, Wilber Pan and Twins to shoot print and TV advertisements to strengthen marketing effects;
- Advertised Xtep brand on the internet through various websites such as www.sportschina.com and www.mop.com, as well as on billboards, buses and bus stops;
- Placed advertisements in fashion magazines, such as Rayli Fashion Pioneer, a nation-wide monthly fashion magazine for women, the audience of which consists primarily of affluent and fashion-conscious women, who are likely to be identified with the brand's daring, bold, and alluring styles.

It is the Group's key strategy to improve our brand image and expand promotion. The advertising and promotional expenses for the period increased to approximately RMB113,110,000, which is about 3 times more than that of the same period last year (2007: RMB28,746,000) and it accounted for approximately 8% of revenue for the period (2007: 5.6%).

## Product design and research and development

The Group believes that superior product design and research and development ("R&D") are crucial factors for success. As a fashion sportswear enterprise, the Group continues to develop innovative design and technology of new products through R&D in order to cater to consumer preferences and respond to market needs. During the period under review, the Group had introduced to the market 1,121 types of footwear designs, 1,347 types of apparel designs and 1,075 types of accessories designs to fulfill different customer demands. The Group has three superior product design teams and one R&D team of more than 381 staff, and also works with world renowned fashion and trend research and design institutions from South Korea, France, and other countries, such as the South Korean-based C&T Fashion Planning and Branding Consultancy Company, to keep abreast of the latest fashion trends so as to formulate suitable design proposals.

As a result of devoting more resources on R&D and design to improve the quality and appearance of our products, the Group's total design and R&D expenses increased to approximately RMB22,511,000 as at 30 June 2008, which is more than 2.4 times than that of the same period last year (2007: approximately RMB6,637,000).

During the period under review, the Group continued to apply the following R&D initiatives in product development:

Footwear:

- Nano-silver anti-bacteria spraying technology — The Group applies this spraying technology to apply nano-silver anti-bacterial chemicals (which are capable of killing 99% of the bacteria on the material on which it is applied) to most of the Group's footwear products. This spraying technology is the result of the Group's research co-operation with the China Academy of Science.
- Fragrance feature — The Group applies a fragrance on most of its footwear products. Such fragrances generally last three to four months and do not affect durability. The Group imports fragrances from suppliers in South Korea and holds the exclusive right to use them on the Group's footwear products in the PRC.

Apparel:

- Starting from the summer of 2008, the Group have been using organic silicone that it intends to import from the United States on one-sided humidity conducive fabrics to make the Group's apparel products more heat-resistant and to preserve the silk screen images that are imprinted on them.

## Strengthen production efficiency

The Group is able to effectively control the costs of production and product quality and respond quickly to changing market demands and fashion trends through the use of its own production facilities. During the period under review, the Group had 12 footwear production lines, and 12 apparel production lines with an annual production capacity of 11 million footwear products and 1 million apparel products, respectively. As the Group's brands are well-received in the market, the utilization rate of the production facilities for the first half of 2008 has reached almost 100%. In order to enhance the cost competitiveness of its current production facilities, the Group is constantly improving and optimizing its production facilities and production lines, reducing stoppages, and improving quality control. During the period under review, the Group has adhered to the established comprehensive quality control system to monitor various processes from design, raw materials procurement and production to delivery, so that Xtep can continue to maintain a quality control level that is beyond that of its peers.

## Financial Review

### Revenue Breakdown

- **Revenue and gross profit margin breakdown by product mix**

| For the six months ended 30 June | 2008 | | | 2007 | | |
|---|---|---|---|---|---|---|
| | RMB'000 | % mix | *Gross profit margin %* | RMB'000 | % mix | *Gross profit margin %* |
| Footwear | 703,567 | 50.0 | *36.1* | 377,572 | 73.6 | *30.9* |
| Apparel | 686,684 | 48.8 | *37.4* | 133,596 | 26.0 | *35.7* |
| Accessories | 17,946 | 1.2 | *35.4* | 2,194 | 0.4 | *32.4* |
| Total | 1,408,197 | 100.0 | *36.8* | 513,362 | 100.0 | *32.2* |

During the period under review, due to the Group's successful brand promotion and the rapid expansion of the retail network operated by our distributors and third-party retailers operate, the revenue from the Group's branded footwear and apparel products grew significantly, with revenue from footwear and apparel increasing by 86.3% and 4 times, respectively as compared to the same period last year. In addition, as the Group shifted its focus from footwear products to allocate more resources to promote and design branded apparel and accessories during the period under review, the Group achieved a more balanced product mix. During the period under review, the percentages of footwear and apparel as a part of total revenue were 50.0% and 48.8%, respectively, as compared to 73.6% and 26.0%, respectively for the same period last year.

During the period under review, the Group's overall gross profit margin also increased as a result of the Group's efforts in branded product development from 32.2% over the same period last year to 36.8%, primarily due to a higher gross profit margin of the Group's branded products than its OEM sales. The gross profit margin of footwear products increased to 36.1% from last year 30.9%, primarily due to the increase in sales of Xtep branded footwear products. The gross profit margin of apparel products grew as well due to the higher gross profit margins of Disney Sport and Koling brand sales, resulting in the increase of gross profit margin of apparel products from 35.7% over the same period last year to 37.4%.

## • Revenue breakdown by branded product sales and OEM Sales

| For the six months ended 30 June | 2008 | | 2007 | |
|---|---|---|---|---|
| | RMB'000 | % mix | RMB'000 | % mix |
| Xtep | 1,308,149 | 92.9 | 438,900 | 85.5 |
| Other brands | 95,047 | 6.7 | – | – |
| Sub-total | 1,403,196 | 99.6 | 438,900 | 85.5 |
| OEM sales | 5,001 | 0.4 | 74,462 | 14.5 |
| Total | 1,408,197 | 100.0 | 513,362 | 100.0 |

During the period under review, Xtep brand remained the main driver of revenue and sales revenue increased by 2 times than that of the same period last year to approximately RMB1,308 million. As the Disney Sport and Koling brands were launched in the market in the second half of 2007, total sales revenue for the period under review amounted to approximately RMB95 million. The Group's revenue from OEM sales was scaled down to account for only 0.4% of the total revenue over the period as the Group had emphasised and allocated more resources to its branded product sales.

## • Revenue breakdown of Xtep brand

| For the six months ended 30 June | 2008 | | 2007 | | Change |
|---|---|---|---|---|---|
| | RMB'000 | % mix | RMB'000 | % mix | |
| Footwear | 662,487 | 50.6 | 303,110 | 69.1 | +118.6% |
| Apparel | 631,586 | 48.3 | 133,596 | 30.4 | +372.8% |
| Accessories | 14,076 | 1.1 | 2,194 | 0.5 | +541.7% |
| Total | 1,308,149 | 100.0 | 438,900 | 100.0 | +198.1% |
| *Gross profit margin* | *36.3%* | | *34.8%* | | *+1.5% pt* |

Leveraging the Group's quickly expanding nationwide distribution network operated by distributors and third-party retailers, Xtep branded footwear and apparel products grew by 1.2 times and 3.7 times for the first half of 2008, as compared to the same period last year, driving the total revenue to increase approximately twofold. The number of retail outlets operated by the Xtep brand's distributors and third-party retailers grew rapidly from 2,860 as at 30 June 2007 to 4,733 as at 30 June 2008, representing an increase of 1,873 retail outlets (equivalent to 65.5%).

On the other hand, to strengthen and balance the product mix between footwear and apparel, the Group allocated more resources to the promotion and increase the types of designs and provide more trendy style and colourful pattern of Xtep branded apparel products. As a result, the percentage mix of Xtep brand footwear and apparel for the period review was 50.6% and 48.3% of the total revenue of Xtep brand products.

The overall gross profit margin of Xtep also increased from 34.8% over the same period last year to 36.3%, due to the optimized product mix and growing sales of higher profit margin apparel products, in addition to the increased average selling price of footwear and apparel products and effective cost control.

## • Volume and Average selling price breakdown of Xtep Brand

| For the six months ended 30 June | | | | |
|---|---|---|---|---|
| | | **2008** | 2007 | Change |
| Footwear | Volume ('000) | 8,834 | 4,397 | +100.9% |
| | Average selling price (RMB) | 75.0 | 68.9 | +8.9% |
| | *Gross profit margin* | *35.5%* | *34.5%* | *+1% pt* |
| Apparel | Volume ('000) | 14,077 | 3,456 | +307.3% |
| | Average selling price (RMB) | 44.9 | 38.7 | +16.1% |
| | *Gross profit margin* | *37.2%* | *35.7%* | *+1.5% pt* |

The increase in the average selling price of footwear and apparel products was mainly due to increased brand recognition and a further increase in retail price, as well as the expansion of the range of product offerings, which allowed for the increase in overall prices of such products. In particular, average selling price of footwear products was up by 8.9% whilst growth of apparel products brand was the most significant, increased by 16.1%. In addition, as sales increased, the Group was able to enhance the bargaining power of the Group to achieve better economies of scale and lower the cost of raw material, the costs of footwear and apparel products during the period only grew by 7.2% and 13.3%. Accordingly, the gross profit margin of footwear and apparel products rose 1% pt and 1.5% pt respectively.

## • Volume and Average selling price breakdown of other brands*

| For the six months ended 30 June 2008 | | |
|---|---|---|
| Footwear | Volume ('000) | 438 |
| | Average selling price (RMB) | 82.4 |
| | *Gross profit margin* | *49.2%* |
| Apparel | Volume ('000) | 723 |
| | Average selling price (RMB) | 76.2 |
| | *Gross profit margin* | *40.1%* |

* Other brands including the Disney Sport and Koling brands, which commence the sales in the second half of 2007. Accordingly, comparable analysis is not applicable to the above table.

The retail outlet of Disney Sport brand and Koling brand increased from 217 and 50 respectively as at 31 December 2007 to 332 and 50 respectively as at 30 June 2008. During the period under review, revenue amounted to RMB95 million and overall gross profit margin was 43.6%. The average selling prices of footwear and apparel products under these two brands were RMB82.4 and RMB76.2, respectively. The high profit margin and average selling price were mainly due to Disney being a world renowned brand with widely known standard characters. In addition, Koling is the Group's high-end brand, designed to appeal to a consumer group that generally has stronger purchasing power and are willing to pay more for the additional style details that characterize this brand.

## • Revenue breakdown by region

| For the six months ended 30 June | 2008 | | 2007 | |
|---|---|---|---|---|
| | RMB'000 | % mix | RMB'000 | % mix |
| Xtep brand | | | | |
| Eastern region | 502,667 | 35.7 | 189,018 | 36.8 |
| Southern region | 389,733 | 27.7 | 105,396 | 20.5 |
| Western region | 187,873 | 13.3 | 65,792 | 12.8 |
| Northern region | 227,876 | 16.2 | 78,694 | 15.4 |
| Sub-total | 1,308,149 | 92.9 | 438,900 | 85.5 |
| Other brands | 95,047 | 6.7 | – | – |
| OEM sales | 5,001 | 0.4 | 74,462 | 14.5 |
| Total | 1,408,197 | 100.0 | 513,362 | 100.0 |

As the distribution network rapidly expanded and with the implementation of effective marketing strategies, the revenue of each region grew multifold for the period under review, particularly in the eastern region and southern region where performance grew by 1.7 times and 2.7 times, respectively, that of the same period last year. The significant growth was mainly due to the increase of number of retail outlets and increase of total sales floor area.

The eastern and southern regions remained the key development areas of the Group, accounting for the largest shares of total revenue, RMB502.7 million and RMB389.7 million, respectively. Hunan, Hubei and Guangdong in the southern region and Jiangsu, Zhejiang, Anhui and Shandong in the eastern region are major expansion provinces as well as the Group's major source of revenue. According to the latest findings released by the China Statistical Bureau, for the first half of 2008, the gross domestic product in Jiangsu, Zhejiang, Anhui, Shandong, Hunan, Hubei and Guangdong provinces grew by 13.6%, 11.4%, 14.2%, 13.8%, 11.8%, 13.9% and 10.7% respectively, over the same period last year. This was higher than the national gross domestic product of 10.4%, demonstrating with huge development potential. Such findings indicate that the Group adopted the correct approach in their development strategies, focusing on such provinces as its key expansion areas. As at 30 June 2008, the number of outlets in these seven provinces amounted to a total of 2,386 retail outlets, accounting for approximately 47% of the nationwide retail network.

- **Average sales per retail outlet of Xtep Brand**

| For the six months ended 30 June | 2008 | | | 2007 | | | |
|---|---|---|---|---|---|---|---|
| | Revenue RMB'000 | Average no. of retail outlets | Average sales per retail outlet RMB | Revenue RMB'000 | Average no. of retail outlets | Average sales per retail outlet RMB | Changes on average sales per retail outlet |
| Eastern region | 502,667 | 1,740 | 288,889 | 189,018 | 934 | 202,483 | 42.7% |
| Southern region | 389,733 | 1,122 | 347,355 | 105,396 | 525 | 200,563 | 73.2% |
| Western region | 187,873 | 799 | 235,136 | 65,792 | 361 | 182,250 | 29.0% |
| Northern region | 227,876 | 895 | 254,610 | 78,694 | 403 | 195,270 | 30.4% |
| Total | 1,308,149 | 4,556 | 287,127 | 438,900 | 2,223 | 197,436 | 45.4% |

- **Cost of sales breakdown**

| For the six months ended 30 June | 2008 | | 2007 | |
|---|---|---|---|---|
| | RMB'000 | % mix | RMB'000 | % mix |
| Raw materials | 451,524 | 50.7 | 205,232 | 58.9 |
| Outsourced production costs | 383,519 | 43.1 | 95,620 | 27.5 |
| Direct staff costs | 45,651 | 5.1 | 42,523 | 12.2 |
| Others | 9,706 | 1.1 | 4,940 | 1.4 |
| Total | 890,400 | 100.0 | 348,315 | 100.0 |

During the period under review, the Group's cost of sales amounted to approximately RMB890.4 million, an increase of 155.6% as compared to RMB348.3 million over the same period last year. As sales volume grew significantly, the Group increased the proportion of outsourced production costs accordingly to effectively lower cost and control the capital expenditure of its production facilities.

### Income tax expense

During the period under review, the income tax of the Group was RMB42,310,000 (2007: RMB10,303,000). The increase of effective tax rate for the period (2008: 14.2%) over the same period last year (2007: 11.3%) was due to certain expenses not deductible for tax and tax loss not recognized. Pursuant to the New Enterprise Income Tax Law of the PRC and its implementation rules (effective from 1 January 2008), both domestic enterprises and foreign-invested enterprises are subject to the unified PRC enterprise income tax rate of 25%. Accordingly, Xtep (China) continues to be entitled to a 50% tax reduction at the unified tax rate of 25% for the years ended 31 December 2008 and 2009 with respect to the new PRC enterprise income tax. Koling (Fujian) Garment Co., Ltd. enjoys exemption from the PRC enterprise income tax for the years ending 31 December 2008 and 2009 and thereafter will be entitled to a 50% reduction in the PRC enterprise income tax for the subsequent three years.

### Profit attributable to equity holders and net profit margin

During the period under review, the profit attributable to equity holders of the Group amounted to RMB254,664,000 (2007: RMB81,077,000), an increase of 214.1% over the same period last year. In addition, the Group's net profit margin rose 2.3% pt to 18.1% as compared to the same period last year (2007: 15.8%) mainly due to the increase in gross margin improvement.

## Dividend

During the period under review, the Board recommended payment of an interim dividend of HK5.0 cents (equivalent to approximately RMB4.4 cents) per Share, totalling HK$110,000,000 (equivalent to approximately RMB96,767,000) for the six months ended 30 June 2008. The total amount of interim dividend represents approximately 38% of the profit attributable to equity holders of the Company.

## Other income and gains

Other income and gains for the period was approximately RMB3,105,000 (2007: RMB680,000). The increase was primarily as a result of increases in rental income, fair value gains on preferred shares and subsidy income from the PRC Government.

## Selling and distribution costs and administrative expenses

As of 30 June 2008, the Group's selling and distribution costs amounted to RMB158,677,000 (2007: RMB46,057,000), which represents 11.3% (2007: 9.0%) of the Group's total revenue. The increase was primarily as a result of the strengthening of Xtep brand marketing during the Olympics to enhance the Group's brand recognition and increased investment in various media channels and advertising. Accordingly, the Group increased its advertising and marketing expenses during the period from RMB28,746,000 for the first half of 2007 (accounting for 5.6% of revenue) to RMB113,110,000 for the first half of 2008 (accounting for 8.0% of revenue). General and administrative expenses increased from RMB23,190,000 for 2007 to RMB61,411,000 for 2008, primarily as a result of the increase in listing fees for the first half of 2008 and the increase in the Group's design and R&D expenses from RMB6,637,000 for the first half of 2007 (accounting for 1.3% of revenue) to RMB22,511,000 for the first half of 2008 (accounting for 1.6% of revenue), mainly due to the investment in the improvement of footwear and apparel products quality, as well as appearance, function and durability.

## Working capital ratio

The Group's average inventory turnover days improved from 68 days for the year ended in 2007 to 58 days during the period under review, primarily as a result of the our increased use of contract manufacturers, and our improved production planning, procurement control and logistics management, thus reducing the inventory level of the Group.

The average trade receivables turnover days reduced from 56 days for the year ended in 2007 to 47 days during the period under review. Such decrease was predominantly due to the strengthening of our credit control and debt collection process that enables us to shorten the debt collection cycle.

The average trade payables turnover days increase from 30 days for the year ended in 2007 to 43 days during the period under review. Such increase was due to improved cash management control and extended credit payment terms to suppliers.

## Liquidity and capital resources

The Group's primary sources of operating funds are cash flow from operating activities and bank borrowings. As at 30 June 2008, the Group's current ratio was 4.4 (31 December 2007: 1.9). The Group maintained a net cash position, reflecting its healthy financial condition, paving the way for future development. As at 30 June 2008, the Group's gearing ratio was 9.4% (31 December 2007: 41.5%), which is defined as total borrowings divided by the sum of share capital and reserves of the Company.

Due to significant improvement of working capital management, the net cash inflow from operating activities for the period ended 30 June 2008 was RMB199.7 million (2007: outflow RMB54.5 million). On the other hand, the Group successfully raised RMB1,872.4 million (net proceed) from Listing and as at 30 June 2008, the Group's total cash and cash equivalents amounted to RMB2,106.0 million (31 December 2007: RMB215.0 million).

## Inventory provision

For the six months ended 30 June 2008, the Group did not have any inventory provision.

## Doubtful debt provision

For the six months ended 30 June 2008, the Group did not have any doubtful debt provision.

## Capital commitments and contingent liabilities

For the six months ended 30 June 2008, the Group did not have any material capital commitments and contingent liabilities.

## Foreign currency risks

The Group mainly operates in the PRC with most of its transactions settled in RMB. The Group's assets and liabilities, and transactions arising from its operations are mainly denominated in RMB. Accordingly, it is believed that the Group has minimal foreign currency risks. The Group has not used any forward contract or currency borrowing to hedge its interest rate risks. However, the management will continue to monitor foreign currency risks and adopt prudent measures as appropriate.

## Significant investments and acquisitions

During the period under review, the Group did not have any significant investments or acquisitions or sales of subsidiaries. The Group continued to seek opportunities to acquire and work with international sportswear products brands in order to generate more returns to its Shareholders.

### Use of net proceeds from the global offer

The shares of the Company were listed on the main board of the Hong Kong Stock Exchange on 3 June 2008 with net proceeds from the global offering of approximately HK$2,088 million (after deducting underwriting commissions and related expenses).

| Use of proceeds | Available to utilize HK$m | Utilized (as at 30 June 2008) HK$m | Unutilized (as at 30 June 2008) HK$m |
|---|---|---|---|
| Media advertising and brand promotion activities | 459 | 40 | 419 |
| Expanding and improving distribution network | 355 | – | 355 |
| Expanding production facilities and operating centre | 397 | – | 397 |
| Acquiring brands | 501 | – | 501 |
| Enhancing design and R&D capabilities | 146 | – | 146 |
| Enhancing IT management system | 63 | – | 63 |
| General working capital | 167 | 10 | 157 |
| Total | 2,088 | 50 | 2,038 |

## Human resources

As of 30 June 2008, the Group had 6,463 employees (31 December 2007: 5,930 employees).

| | As at 30 June 2008 | As at 31 December 2007 |
|---|---|---|
| Sales and marketing | 366 | 316 |
| Product design, research and development | 381 | 371 |
| Management and administrative, finance and quality control | 477 | 455 |
| Production | 5,239 | 4,788 |
| Total | 6,463 | 5,930 |

The Group provides introductory orientation programs and continuous training to its employees that cover industry overview, technology and product knowledge, industry quality standards and work safety standards to enhance the service quality and of its staff. The Group will strive to strengthen human resources management to provide strong support for the development of the Group's business through staff recruitment initiatives and the optimization of the development of its organizational structure and corporate culture to ensure that the Group will be able to maintain sustainable and fast-growing development in the future.

## Prospects

### Market outlook

The Beijing 2008 Olympic Games held in August 2008 have stirred up sports frenzy in China. Benefiting from the future economic growth of China and the growing consumption power of Chinese citizens, the sportswear product industry is expected to extend its growth after the Olympics. Meanwhile, leveraging its position as the industry leader, the Group will capture the opportunities generated after the Olympics to enhance brand competitiveness of its brand and to further expand its growth horizons.

### Optimizing and expanding sales network

Given the increasing emphasis on the fashion sportswear product market among citizens, the Group will continue to optimize its own sales network, including expansion in size of retail outlets, re-renovation and enhancement of its management system, strengthening its support of retail terminals as appropriate so as to increase the Xtep brand's market penetration. For the full year of 2008 expansion plan of sales network, Xtep and Disney Sport brands plan to open a total of 1,100 outlets and increase a total of approximately 100,000 sqm of sales floor area, so as to increase the average saleable area of retail outlets and overall profitability.

The Group considers that the establishment of flagship stores is also a key approach to brand building. Therefore, we identify strategic and prime locations for flagship stores selling our Xtep branded products. There are currently 3 flagship stores which are operated and managed by our distributors, these flagship stores are located in Changsha (occupying a store area of approximately 3,000 sqm), Wuhan (occupying a store area of approximately 2,000 sqm), and Hefei (occupying a store area of approximately 2,000 sqm). Our current plan is to identify a total of approximately 10 strategic locations in 2008 to open these flagship stores.

### Enhancing brand recognition

Looking ahead, the Group will continue to appoint brand representatives to further reinforce the Xtep brand to the general public through entertainment-driven sports. Following this strategy, the Group will sponsor approximately 10 concerts titled "特步五星演唱會" (Xtep's Five Stars Concert) which will be held in the major cities in the PRC in 2009 and the celebrities will be wearing Xtep brand's footwear and apparel throughout all the concerts. The Group will also be the title sponsor of the 2008 Pingpang Carnival, a high-profile TV show on Hunan Satellite TV organised by the International Table Tennis Federation, the Chinese Table Tennis Association and Hunan Satellite TV, and broadcast through Hunan Satellite TV. In addition, the Group will continue to pursue its marketing strategies of sports sponsorships in order to maintain the popularity of sports after the Olympics. The Group will be the sole sports product partner for "2008 西安城墻國際馬拉松賽" (2008 Xian International Marathon) to be held on 1 November 2008 and the 11th National Games of China in 2009.

### Consolidating multi-brand strengths

Xtep currently operates the Xtep, Disney Sport and Koling brands. The Group's three differentiated brands share the common goal of providing fashion in addition to sports functionality. Leveraging its multi-brand strengths, together with its premier and innovative technology, the Group launches a variety of new products targeting different customer groups in order to expand its market share in China. In addition, the Group also actively seeks opportunities to cooperate with other brand suppliers to continue to expand the domestic fashion sportswear product business. Combining the strengths of different brands, the Group strongly believes that the strategy of combining the strengths of other brands with the Group's existing brands and business and are in the interest of its future development.

### Strengthening design and R&D capabilities

Enhancing design and R&D capabilities is another core element of the Group's future development. The Group will gather domestic and overseas design and R&D professionals to launch a variety of new products and technologies that cater to customers' needs, including X-太極減震科技(X-polar shock resistant technology), X-波紋回旋減震科技 (X-wave whirling shock resistant technology), X-DRIVER power technology, bionic technology functions, and the eco-friendly materials project in relation to Dannier "breathing" fabrics technology with Dannier. Moreover, the Group will also launch limited editions of footwear and apparel products and accessories relating to brand representatives such as Jolin Tsai series and Wilber Pan series so as to equip the Group's products with both function and fashionable design.

### Expanding DRP system coverage

In order to enhance and strengthen the management of distributors and terminal retailers, and effectively conduct systematic analysis of the purchase of the Group's branded products by terminal customers, the Group will expand the coverage of the DRP management system amongst terminal retailers. Such coverage is expected to increase from approximately 25% currently to approximately 30% at the end of 2008.

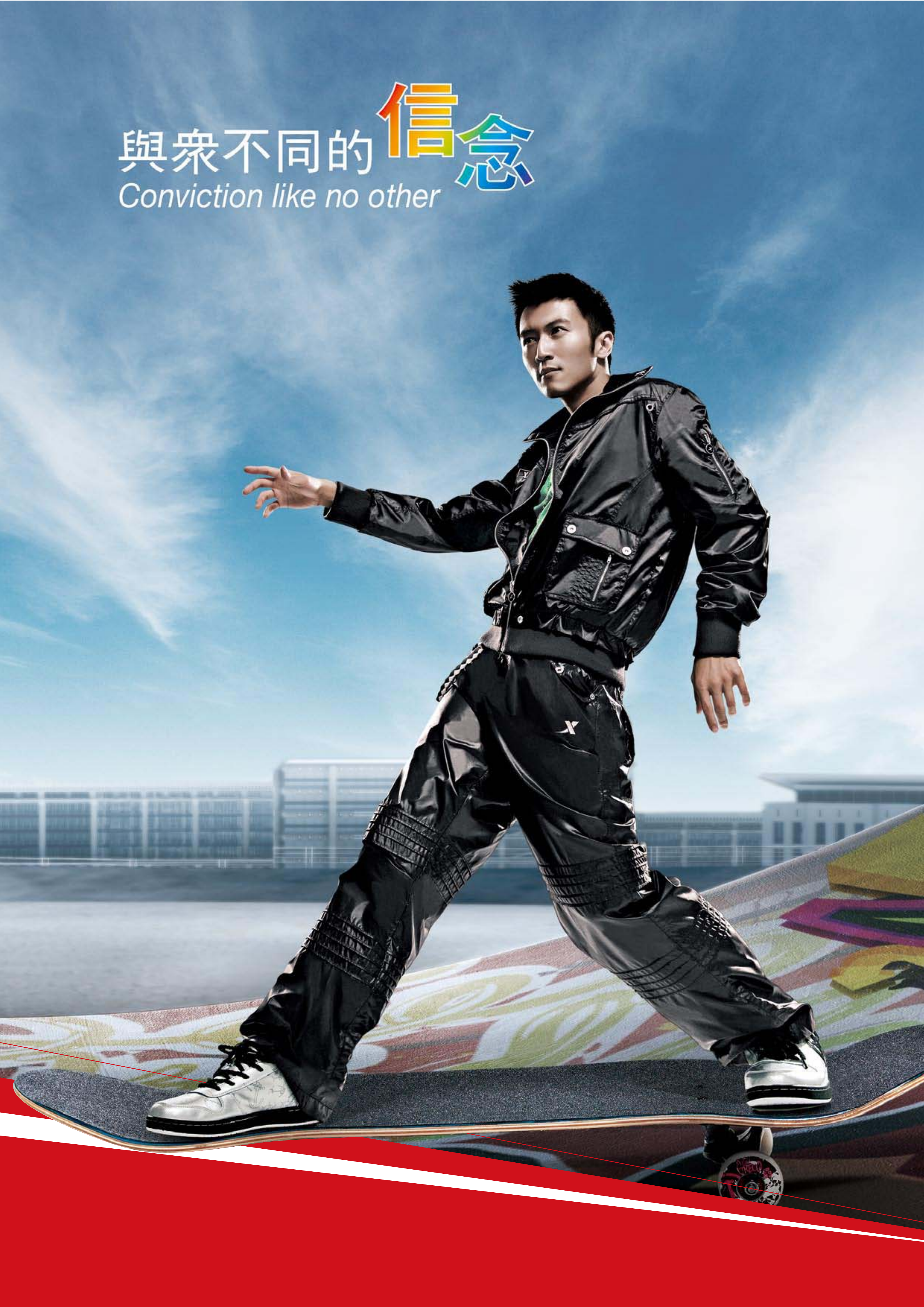
## Investor Relations

The Group strongly believes that investor relations are crucial to a listed company. Maintaining sound relationships with investors and keeping them abreast of the latest corporate communications and business development in a timely manner enhances the transparency and corporate governance of the Group, thus strengthening the Group's corporate position. The Group's chief financial officer and company secretary, Mr. Ho Yui Pok, Eleutherius is responsible for the investor relations of the Group, fully supported by the Board and the senior management team. During the period under review, the Group actively participated in various investor relations-related activities and started an investor relations column on the company website so as to provide real-time information to its investors.

Shares of the Company was listed on the main board of the Hong Kong Stock Exchange on 3 June 2008. During its global roadshow, the Group actively engaged in meetings with global investors to introduce the Group's corporate strengths and growth strategies to gain support and recognition from market and institutional investors. Meanwhile, the Group also received valuable advice and feedback from its exchanges with many investors, while focusing on understanding their concerns. Since its Listing, the Group has continued to maintain sound communications with its investors, attending investor conferences, one-on-one meetings and call conferences. The Group has also participated in investor forums, press conferences and media interviews so as to enable its Shareholders, investors, and analysts to grasp the latest real-time updates and business development strategies of the Company.

## Conclusion

The sportswear products market in China is fiercely competitive. To differentiate itself from its peers, distinguished marketing strategies are crucial. The Group grew rapidly during the period and attained satisfactory performance in terms of its sales and retail distribution network, which maintaining its position as industry leader. The Group strives to become a premier fashion sportswear products enterprise in China. Leveraging its in depth experience in the domestic fashion sportswear products, innovative design and R&D capabilities, and multi-brand strengths, Xtep is determined to further increase its brand competitiveness to generate excellent results in the future.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# Corporate Governance and Other Information

## Corporate Governance Practices

Good corporate governance is conducive to enhancing overall performance and accountability and is essential in modern corporate administration. The Board continuously observe the principles of good corporate governance in the interests of Shareholders and devotes considerable effort to identifying and formalizing best practice.

The Company has adopted the Corporate Governance Code set out in Appendix 14 to the Listing Rules. The Company has complied with the Corporate Governance Code throughout the six months ended 30 June 2008 except for the deviation from code provision A.2.1, which stipulates that the roles of the chairman and chief executive officer should be separate and should not be performed by the same individual.

The Group does not at present separate the roles of the chairman and chief executive officer. Mr. Ding Shui Po is the chairman and chief executive officer of the Group. He has extensive experience in sportswear industry and is responsible for the overall corporate strategies, planning and business management of the Group. The Board considers that vesting the roles of chairman and chief executive officer in the same individual is beneficial to the business prospects and management of the Group. The balance of power and authorities is ensured by the operation of the Board and the senior management, which comprise experienced and high calibre individuals. The Board currently comprises five executive Directors, one non-executive Director and three independent non-executive Directors and has a strong independence element in its composition.

## Model Code

The Company has also adopted the Model Code set out in Appendix 10 of the Listing Rules as its code of conduct regarding securities transactions by the Directors. Having made specific enquiry with all Directors of the Company, all Directors confirmed that they have complied with the required standard set out in the Model Code throughout the six months ended 30 June 2008.

## Audit Committee

The Company established an audit committee pursuant to a resolution of the Directors passed on 7 May 2008 in compliance with Rule 3.21 of the Listing Rules. The primary duties of the audit committee are mainly to make recommendation to the Board on the appointment and removal of external auditor, review the financial statements and material advice in respect of financial reporting, and oversee the internal control procedures of the Company. The audit committee consists of three members, namely, Mr. Sin Ka Man, Mr. Xu Peng Xiang and Dr. Gao Xian Feng, all of whom are independent non-executive Directors. Mr. Sin Ka Man is the chairman of the audit committee. The audit committee has held meetings to discuss the auditing, internal controls and financial reporting matters of the Company, including the review of the interim report and the unaudited interim financial statements for the six months ended 30 June 2008.

## Remuneration Committee

The Company established a remuneration committee on 7 May 2008 with written terms of reference. The primary duties of the remuneration committee are to make recommendation to the Board on the overall remuneration policy and structure relating to all Directors and senior management of the Company, review performance based remuneration, and ensure none of the Directors determine their own remuneration. The remuneration committee consists of three members, namely, Mr. Xu Peng Xiang, Dr. Gao Xian Feng (both are independent non-executive Directors) and Ms. Ding Mei Qing, an executive Director. Mr. Xu Peng Xiang is the chairman of the remuneration committee.

## Nomination committee

The Company established a nomination committee on 7 May 2008 with written terms of reference. The primary functions of the nomination committee are to make recommendations to the Board regarding candidates to fill vacancies on the Board. The nomination committee consists of three members, namely, Mr. Ding Shui Po, the Group's chairman and two independent non-executive Directors, namely, Mr. Xu Peng Xiang and Dr. Gao Xian Feng. Mr. Ding Shui Po is the chairman of the nomination committee.

## Purchase, Sale or Redemption of The Company's Listed Securities

The shares of the Company were listed on the Hong Kong Stock Exchange on 3 June 2008. Neither the Company nor any of its subsidiaries has purchased, sold or redeemed any of the Company's listed securities during the six months ended 30 June 2008.

## Disclosure of Interests

### Directors' and chief executives' interests and short positions in shares, underlying shares and debentures

As at 30 June 2008, the directors and the chief executives of the Company and their respective associates had the following interests or short positions in the shares, underlying shares and debentures of the Company and its associated corporations (within the meaning of Part XV of the SFO ), as recorded in the register required to be kept under Section 352 of the SFO or as otherwise notified to the Company and the Hong Kong Stock Exchange pursuant to the Model Code:

*Long positions in the Company*

| Name of Director | Nature of interest | Number of shares interested | Approximate percentage of interest in the issued share capital of the Company |
|---|---|---|---|
| Mr. Ding Shui Po (1) | Interests of controlled corporation | 1,418,059,500 | 64.50% |
| Ms. Ding Mei Qing (2) | Interests of controlled corporation | 1,418,059,500 | 64.50% |
| Mr. Lin Zhang Li (3) | Interests of spouse | 1,418,059,500 | 64.50% |
| Mr. Ye Qi (4) | Beneficial interests | 1,500,000 | 0.07% |

Notes:

(1) Mr. Ding Shui Po is deemed to be interested in the shares of the Company held by Group Success by virtue of it being controlled by Mr. Ding Shui Po.

(2) Ms. Ding Mei Qing is deemed to be interested in the shares of the Company held by Group Success by virtue of Group Success being controlled by Ms. Ding Mei Qing.

(3) Mr. Lin Zhang Li, the husband of Ms. Ding Mei Qing and an executive Director, is deemed to be interested in his wife's interests in Group Success.

(4) These shares are subject to the exercise of options granted under a pre-IPO share option scheme of the Company adopted by the Shareholders of the Company on 7 May 2008 and 0.07% is the percentage of enlarged issue share capital of the Company after full exercise of the Pre-IPO Share Option.

Save as disclosed above, as at 30 June 2008, none of the directors or chief executives of the Company had or was deemed to have any interests or short position in the shares, underlying shares or debentures of the Company and its associated corporations (within the meaning of Part XV of the SFO), which had been recorded in the register maintained by the Company pursuant to section 352 of the SFO or which had been notified to the Company and the Stock Exchange pursuant to the Model Code.

At no time was the Company, or any of its holding companies, its subsidiaries or its fellow subsidiaries a party to any arrangement to enable the directors and chief executives of the Company (including their spouse and children under 18 years of age) to hold any interest or short positions in the shares or underlying shares in, or debentures of, the Company or its associated corporations (within the meaning of Part XV of the SFO).

### Substantial Shareholders' interests and short positions in shares and underlying shares

As at 30 June 2008, the persons or corporations (not being a director or chief executive of the Company) who have interest or short positions in the shares and underlying shares of the Company as recorded in the register required to be kept under section 336 of the SFO were as follows:

| Name of Shareholders | Nature of Interest | Number of shares interested | Approximate percentage of interest in the issued share capital of the Company |
|---|---|---|---|
| Group Success | Beneficial interests | 1,418,059,500 | 64.50% |
| Carlyle Asia Growth Partners III, L.P. | Beneficial interests | 176,864,909 | 8.04% |
| CAGP III Co-investment, L.P. | Beneficial interests | 7,054,591 | 0.32% |
| CAGP General Partner, L.P. | Interests of controlled corporation [(1)] | 183,919,500 | 8.36% |
| CAGP Ltd | Interests of controlled corporation [(1)] | 183,919,500 | 8.36% |

Note:

(1) CAGP General Partner, L.P. is the general partner of Carlyle Asia Growth Partners III, L.P. and CAGP III Co-investment, L.P., both limited partnerships. CAGP Ltd is the general partner of CAGP General Partner, L.P.

Save as disclosed above, as at 30 June 2008, the directors of the Company are not aware of any other person or corporation having an interest or short position in shares and underlying shares of the Company which would require to be recorded in the register required to be kept by the Company pursuant to Section 336 of the SFO.


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# Condensed Consolidated Income Statement

*Six months ended 30 June 2008*

| | Notes | (Unaudited) Six months ended 30 June 2008 RMB'000 | (Unaudited) Six months ended 30 June 2007 RMB'000 |
|---|---|---|---|
| **REVENUE** | 4 | 1,408,197 | 513,362 |
| Cost of sales | | (890,400) | (348,315) |
| **Gross profit** | | 517,797 | 165,047 |
| Other income and gains | 5 | 3,105 | 680 |
| Selling and distribution costs | | (158,677) | (46,057) |
| General and administrative expenses | | (61,411) | (23,190) |
| **Operating Profit** | 6 | 300,814 | 96,480 |
| Interest income | | 2,786 | 138 |
| Finance costs | 7 | (6,626) | (5,238) |
| **PROFIT BEFORE TAX** | | 296,974 | 91,380 |
| Tax | 8 | (42,310) | (10,303) |
| **PROFIT FOR THE PERIOD** | | 254,664 | 81,077 |
| Interim dividend | 9 | 96,767 | – |
| **EARNINGS PER SHARE ATTRIBUTABLE TO EQUITY HOLDERS OF THE COMPANY** | 10 | | |
| – Basic (RMB cents) | | 16.01 | 5.52 |
| – Diluted (RMB cents) | | 14.63 | 5.51 |

# Condensed Consolidated Balance Sheet

*30 June 2008*

| | Notes | (Unaudited) 30 June 2008 RMB'000 | (Audited) 31 December 2007 RMB'000 |
|---|---|---|---|
| **NON-CURRENT ASSETS** | | | |
| Property, plant and equipment | | 102,421 | 96,585 |
| Prepaid land lease payments | | 22,098 | 21,763 |
| Deposit paid | 11 | – | 10,000 |
| Intangible assets | | 258 | 289 |
| | | 124,777 | 128,637 |
| **CURRENT ASSETS** | | | |
| Inventories | 12 | 372,521 | 193,505 |
| Trade and bills receivables | 13 | 485,059 | 234,383 |
| Prepayments, deposits and other receivables | 14 | 61,659 | 131,984 |
| Financial assets at fair value through profit or loss | 15 | 175,912 | – |
| Pledged bank balances | 16 | 5,400 | – |
| Cash and cash equivalents | 16 | 2,106,043 | 215,018 |
| | | 3,206,594 | 774,890 |
| **CURRENT LIABILITIES** | | | |
| Trade and bills payables | 17 | 362,000 | 55,859 |
| Deposits received, other payables and accruals | 18 | 88,573 | 41,102 |
| Interest-bearing bank borrowings | 19 | 243,000 | 116,000 |
| Due to a director | 20 | – | 32,874 |
| Dividend payable | | – | 129,455 |
| Tax payable | | 39,851 | 30,518 |
| | | 733,424 | 405,808 |
| **NET CURRENT ASSETS** | | 2,473,170 | 369,082 |
| **TOTAL ASSETS LESS CURRENT LIABILITIES** | | 2,597,947 | 497,719 |
| **NON-CURRENT LIABILITIES** | | | |
| Preferred shares | 21 | – | 216,599 |
| Derivative component of preferred shares | 21 | – | 1,324 |
| | | – | 217,923 |
| Net assets | | 2,597,947 | 279,796 |
| **EQUITY** | | | |
| Equity attributable to equity holders of the Company | | | |
| Issued share capital | 22 | 19,409 | 936 |
| Reserves | 23 | 2,578,538 | 278,860 |
| Total equity | | 2,597,947 | 279,796 |

# Condensed Consolidated Statement Of Changes In Equity

*Six months ended 30 June 2008*

## Six months ended 30 June 2008 (unaudited)

| | Notes | Attributable to equity holders of the Company | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | | Issued share capital RMB'000 | Share premium account RMB'000 | Capital reserve RMB'000 | Statutory surplus funds RMB'000 | Share option reserve RMB'000 | Exchange fluctuation reserve RMB'000 | Retained profits RMB'000 | Total reserves RMB'000 | Total equity RMB'000 |
| At 1 January 2008 (Audited) | | 936 | – | 118,600 | 46,116 | – | 3,463 | 110,681 | 278,860 | 279,796 |
| Exchange realignment | | – | – | – | – | – | 3,454 | – | 3,454 | 3,454 |
| Total income and expenses directly recognised in equity | | – | – | – | – | – | 3,454 | – | 3,454 | 3,454 |
| Profit for the period | | – | – | – | – | – | – | 254,664 | 254,664 | 254,664 |
| Total income and expense for the period | | – | – | – | – | – | 3,454 | 254,664 | 258,118 | 258,118 |
| Conversion of preferred shares into ordinary shares | 22(b)(iv), 22(b)(v) | 109 | 216,897 | – | – | – | – | – | 216,897 | 217,006 |
| Capitalisation issue | 22(b)(vi) | 13,526 | (13,526) | – | – | – | – | – | (13,526) | – |
| Issue of Pre-IPO Share Options | 24 | – | – | – | – | 921 | – | – | 921 | 921 |
| Issue of ordinary shares | 22(b)(vii) | 4,838 | 1,954,693 | – | – | – | – | – | 1,954,693 | 1,959,531 |
| Share issue expenses | | – | (117,425) | – | – | – | – | – | (117,425) | (117,425) |
| At 30 June 2008 (Unaudited) | | 19,409 | 2,040,639 | 118,600 | 46,116 | 921 | 6,917 | 365,345 | 2,578,538 | 2,597,947 |

*Six months ended 30 June 2008*

## Six months ended 30 June 2007 (unaudited)

| | Notes | Issued share capital RMB'000 | Share premium account RMB'000 | Capital reserve RMB'000 | Statutory surplus funds RMB'000 | Share option reserve RMB'000 | Exchange fluctuation reserve RMB'000 | Retained profits RMB'000 | Total reserves RMB'000 | Total equity RMB'000 |
|---|---|---|---|---|---|---|---|---|---|---|
| | | Attributable to equity holders of the Company | | | | | | | | |
| At 1 January 2007 (Audited) | | 122,993 | – | – | 10,719 | – | – | 53,655 | 64,374 | 187,367 |
| Exchange realignment | | – | – | – | – | – | 353 | – | 353 | 353 |
| Total income and expenses directly recognised in equity | | – | – | – | – | – | 353 | – | 353 | 353 |
| Profit for the period | | – | – | – | – | – | – | 81,077 | 81,077 | 81,077 |
| Total income and expenses for the period | | – | – | – | – | – | 353 | 81,077 | 81,430 | 81,430 |
| Increase in paid-up capital of subsidiaries | | 34,701 | – | – | – | – | – | – | – | 34,701 |
| Issue of shares the Company | 22(b)(i), 22(b)(ii) | – | – | – | – | – | – | – | – | – |
| Acquisition of subsidiaries pursuant of Group Reorganisation | | (157,694) | – | 157,694 | – | – | – | – | 157,694 | – |
| At 30 June 2007 (Unaudited) | | – | – | 157,694 | 10,719 | – | 353 | 134,732 | 303,498 | 303,498 |

# Condensed Consolidated Cash Flow Statement

*Six months ended 30 June 2008*

| | (Unaudited) Six months ended 30 June 2008 RMB'000 | (Unaudited) Six months ended 30 June 2007 RMB'000 |
|---|---|---|
| CASH INFLOW/(OUTFLOW) FROM OPERATING ACTIVITIES | 199,744 | (54,509) |
| CASH FLOWS FROM INVESTING ACTIVITIES | | |
| Purchases of items of property, plant and equipment | (10,986) | (15,243) |
| Additions to prepaid land lease payments | (579) | – |
| Proceeds from disposal of items of property, plant and equipment | – | 50 |
| Decrease in deposit paid | 10,000 | – |
| Increase in financial assets at fair value through profit or loss | (175,912) | – |
| Decrease in pledged time deposits | – | 7,880 |
| Decrease in loan receivables | – | 15,000 |
| Exchange realignment | 3,880 | 353 |
| Net cash inflow/(outflow) from investing activities | (173,597) | 8,040 |
| CASH FLOWS FROM FINANCING ACTIVITIES | | |
| Increase in paid-in capital of subsidiaries | – | 34,701 |
| New bank loans | 127,000 | 27,000 |
| Issue of convertible bonds | – | 40,000 |
| Issue of ordinary shares, net | 1,872,441 | – |
| Dividend paid | (129,455) | – |
| Interest received | 719 | – |
| Net cash inflow from financing activities | 1,870,705 | 101,701 |
| NET INCREASE IN CASH AND CASH EQUIVALENTS | 1,896,852 | 55,232 |
| Cash and cash equivalents at beginning of period | 215,018 | 22,216 |
| Effects of foreign exchange rate changes, net | (427) | – |
| Cash and cash equivalents at end of period | 2,111,443 | 77,448 |
| ANALYSIS OF BALANCES OF CASH AND CASH EQUIVALENTS | | |
| Cash and bank balances | 743,842 | 77,448 |
| Pledged bank balances | 5,400 | – |
| Non-pledged time deposits with original maturity of less than three months when acquired | 1,362,201 | – |
| | 2,111,443 | 77,448 |

# Notes To Condensed Consolidated Interim Financial Statements

*Six months ended 30 June 2008*

## 1. CORPORATE INFORMATION AND GROUP REORGANISATION

The Company is a limited liability company incorporated in the Cayman Islands on 10 April 2007. The Company's principal place of business in Hong Kong is located at Suite 2401-02, Shui On Centre, 6-8 Harbour Road, Wanchai, Hong Kong.

Pursuant to the group reorganisation (the "Group Reorganisation") as more fully described in the section headed "History and Corporate Structure" in the prospectus of the Company dated 21 May 2008 (the "Prospectus") and in Appendix VI "Statutory and General Information" to the Prospectus pursuant to the listing (the "Listing") on the Main Board of The Stock Exchange of Hong Kong Limited (the "Stock Exchange"), the Company became the holding company of the subsidiaries now comprising the Group on 19 September 2007.

The shares of the Company were listed on the Stock Exchange on 3 June 2008 (the "Listing Date").

During the period, the Company and its subsidiaries (the "Group") were engaged in the design, development, manufacture and marketing of sportswear, including footwear, apparel and accessory products, sold under the Xtep brand, the Disney Sport brand and the Koling brand.

## 2.1 BASIS OF PRESENTATION

The Group Reorganisation involved business combination of entities under common control and the Group is regarded and accounted for as a continuing group. Accordingly, the condensed consolidated interim financial statements have been prepared in accordance with the principles of merger accounting as if the current group structure resulting from the Group Reorganisation had been in existence beginning 1 January 2007 or since the respective dates of their incorporation or establishment, where this is a shorter period. All significant intra-group transactions and balances have been eliminated on consolidation.

## 2.2 BASIS OF PREPARATION

The interim financial statements contain the condensed consolidated balance sheet of the Group as at 30 June 2008, condensed consolidated income statements, condensed consolidated statements of changes in equity and condensed consolidated cash flow statements of the Group for the six months ended 30 June 2008 and 2007, and selected explanatory notes (the "Condensed Consolidated Interim Financial Statements"). The notes include an explanation of events and transactions that are significant to an understanding of the changes in financial position and performance of the Group since the Company's accountants' report (the "Accountants' Report") as set out in Appendix I to the Prospectus. The interim financial statements and notes thereon do not include all of the information required for a full set of financial statements prepared in accordance with Hong Kong Financial Reporting Standards ("HKFRSs"). The Condensed Consolidated Interim Financial Statements have been prepared in accordance with Hong Kong Accounting Standard ("HKAS") 34 "Interim Financial Reporting" issued by the Hong Kong Institute of Certified Public Accountants ("HKICPA").

The Condensed Consolidated Interim Financial Statements are presented in Renminbi ("RMB"), rounded to the nearest thousand, on the historical cost basis, except for financial assets at fair value through profit or loss, which have been measured at fair value.

## 2.3 SIGNIFICANT ACCOUNTING POLICIES

The significant accounting policies adopted in the preparation of the Condensed Consolidated Interim Financial Statements are consistent with those used by management in the preparation of the financial information summarised in the Accountants' Report. Accordingly, the Condensed Consolidated Interim Financial Statements should be read in conjunction with the Accountants' Report. The accounting policies adopted in relation to financial assets at fair value through profit or loss and share-based payment, which are applicable for the six months ended 30 June 2008 are summarised below:

### Financial assets at fair value through profit or loss

Financial assets at fair value through profit or loss include financial assets held for trading. Financial assets are classified as held for trading if they are acquired for the purpose of sale in the near term. Gains or losses on investments held for trading are recognised in the income statement. The net fair value gain or loss recognised in the income statement does not include any dividends or interest earned on these financial assets, which are recognised in accordance with the policy set out for "Revenue recognition" in the Accountants' Report.

The fair value of investments that are actively traded in organised financial markets is determined by reference to quoted market bid prices at the close of business at the balance sheet date. For investments where there is no active market, fair value is determined using valuation techniques. Such techniques include using recent arm's length market transactions; reference to the current market value of another instrument which is substantially the same; a discounted cash flow analysis; and option pricing models.

### Employee benefits

*Share-based payment transactions*

The Company operates two share option schemes for the purpose of providing incentives and rewards to eligible participants who contribute to the success of the Group's operations. Employees (including directors) of the Group receive remuneration in the form of share-based payment transactions, whereby employees render services as consideration for equity instruments ("equity-settled transactions").

The cost of equity-settled transactions with employees is measured by reference to the fair value at the date at which they are granted. The fair value is determined by an external professional qualified valuer using an appropriate pricing model, further details of which are given in note 24 to the Condensed Consolidated Interim Financial Statements. In valuing equity-settled transactions, no account is taken of any performance conditions, other than conditions linked to the price of the shares of the Company ("market conditions"), if applicable.

The cost of equity-settled transactions is recognised, together with a corresponding increase in equity, over the period in which the performance and/or service conditions are fulfilled, ending on the date on which the relevant employees become fully entitled to the award (the "vesting date"). The cumulative expense recognised for equity-settled transactions at each balance sheet date until the vesting date reflects the extent to which the vesting period has expired and the Group's best estimate of the number of equity instruments that will ultimately vest. The charge or credit to the income statement for a period represents the movement in the cumulative expense recognised as at the beginning and end of that period.

No expense is recognised for awards that do not ultimately vest, except for awards where vesting is conditional upon a market condition, which are treated as vesting irrespective of whether or not the market condition is satisfied, provided that all other performance conditions are satisfied.

Where the terms of an equity-settled award are modified, as a minimum an expense is recognised as if the terms had not been modified. In addition, an expense is recognised for any modification, which increases the total fair value of the share-based payment arrangement, or is otherwise beneficial to the employee as measured at the date of modification.

Where an equity-settled award is cancelled, it is treated as if it had vested on the date of cancellation, and any expense not yet recognised for the award is recognised immediately. However, if a new award is substituted for the cancelled award, and is designated as a replacement award on the date that it is granted, the cancelled and new awards are treated as if they were a modification of the original award, as described in the previous paragraph.

The dilutive effect of outstanding options is reflected as additional share dilution in the computation of earnings per share.

## 2.4 IMPACT OF NEW AND REVISED HONG KONG FINANCIAL REPORTING STANDARDS

During the six months ended 30 June 2008, the Group has applied, for the first time, the following new and revised HKFRSs (which include all HKFRSs, HKASs and Interpretations) issued by the HKICPA which are relevant to the Group and effective for the accounting periods beginning on or after 1 January 2008:

| | |
|---|---|
| HK(IFRIC) – Int 11 | HKFRS 2 - Group and Treasury Share Transactions |
| HK(IFRIC) – Int 12 | Service Concession Arrangements |
| HK(IFRIC) – Int 14 | HKAS 19 - The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction |

The application of the above revised Interpretations has had no material impact on the accounting policies of the Group and the methods of computation in the Condensed Consolidated Interim Financial Statements.

## 2.5 IMPACT OF ISSUED BUT NOT YET EFFECTIVE HONG KONG FINANCIAL REPORTING STANDARDS

The Group has not applied the following new and revised HKFRSs, that have been issued but are not yet effective, in the Condensed Consolidated Interim Financial Statements.

| | |
|---|---|
| HKFRS 2 Amendment | Share-based Payment: Vesting Conditions and Cancellations[1] |
| HKFRS 3 (Revised) | Business Combinations[2] |
| HKFRS 8 | Operating Segments[1] |
| HKAS 1 (Revised) | Presentation of Financial Statements[1] |
| HKAS 23 (Revised) | Borrowing Costs[1] |
| HKAS 27 (Revised) | Consolidated and Separate Financial Statements[2] |
| HKAS 32 and HKAS 1 Amendment | Puttable Financial Instruments and Obligations Arising on Liquidation[1] |
| HK(IFRIC)-Int 13 | Customer Loyalty Programmes[3] |

[1] Effective for annual periods beginning on or after 1 January 2009
[2] Effective for annual periods beginning on or after 1 July 2009
[3] Effective for annual periods beginning on or after 1 July 2008

The Group is in the process of making an assessment of the impact of these new and revised HKFRSs upon initial application. So far, it has concluded that while the adoption of HKAS 1 (Revised) and HKFRS 8 may result in new or amended disclosures, these new and revised HKFRSs are unlikely to have a significant impact on the Group's results of operations and financial position.

## 2.6 SIGNIFICANT ACCOUNTING ESTIMATES

The preparation of the Condensed Consolidated Interim Financial Statements in conformity with HKAS 34 requires management to make judgements, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities, income and expenses on a year to date basis. Actual results may differ from these estimates.

In preparing the Condensed Consolidated Interim Financial Statements, the significant judgements made by management in applying the Group's accounting policies and key sources of estimation uncertainty were the same as those used by management in the preparation of the financial information summarised in the Accountants' Report. The estimation uncertainty made by management in relation to share-based payment, which is applicable for the six months ended 30 June 2008 is summarised below:

**Valuation of share options**

As described in note 24 to the Condensed Consolidated Interim Financial Statements, the Company has engaged an independent professional qualified valuer to assist in the valuation of the share options granted during the period. The fair value of options granted under the share option scheme is determined using the Black-Scholes-Merton Option Pricing Model. The significant inputs into the model were weighted average share price at grant date, risk-free interest rate, exercise price, expected volatility of the underlying shares, expected dividend yield and expected life of options. When the actual results of the inputs differ from management's estimate, it will have an impact on share option expenses and the related share option reserve of the Company. As at 30 June 2008, the fair value of the share options granted by the Company was RMB11,051,000, of which the share option expense of RMB921,000 was recognised during the six months ended 30 June 2008.

## 3. SEGMENT INFORMATION

The Group is principally engaged in the manufacture and sale of sportswear, including footwear, apparel and accessories. All of the Group's products are of a similar nature and subject to similar risk and returns. Accordingly, the Group's operating activities are attributable to a single business segment.

In addition, the Group's revenue, expenses, results, assets and liabilities and capital expenditures are predominantly attributable to a single geographical region, which is the People's Republic of China (the "PRC"). Therefore, no analysis in business or geographical segment is presented.

*30 June 2008*

## 4. REVENUE

Revenue, which is also the Group's turnover, represents the net invoiced value of goods sold during the period, after allowances for returns and trade discounts.

An analysis of revenue is as follows:

| | (Unaudited) Six months ended 30 June 2008 RMB'000 | (Unaudited) Six months ended 30 June 2007 RMB'000 |
|---|---|---|
| Footwear | 703,567 | 377,572 |
| Apparel | 686,684 | 133,596 |
| Accessories | 17,946 | 2,194 |
| | 1,408,197 | 513,362 |

## 5. OTHER INCOME AND GAINS

| | (Unaudited) Six months ended 30 June 2008 RMB'000 | (Unaudited) Six months ended 30 June 2007 RMB'000 |
|---|---|---|
| Rental income | 288 | 60 |
| Subsidy income from the PRC government | 770 | 350 |
| Fair value gain on derivative component of preferred shares | 1,156 | – |
| Others | 891 | 270 |
| | 3,105 | 680 |

## 6. OPERATING PROFIT

The Group's operating profit is arrived at after charging:

| | (Unaudited) Six months ended 30 June 2008 RMB'000 | (Unaudited) Six months ended 30 June 2007 RMB'000 |
|---|---|---|
| Research and development costs | 22,511 | 6,637 |
| Staff costs | 74,643 | 51,524 |
| Depreciation | 5,150 | 3,599 |
| Amortisation of intangible assets | 31 | 43 |
| Amortisation of prepaid land lease payments | 251 | 245 |
| Advertising and promotion costs | 113,110 | 28,746 |

## 7. FINANCE COSTS

| | (Unaudited) Six months ended 30 June 2008 RMB'000 | (Unaudited) Six months ended 30 June 2007 RMB'000 |
|---|---|---|
| Interest on bank loans repayable within five years | 6,387 | 5,238 |
| Interest expense on preferred shares | 239 | – |
| | 6,626 | 5,238 |

## 8. TAX

No provision for Hong Kong profits tax has been made as the Group did not generate any assessable profits arising in Hong Kong during the period (six months ended 30 June 2007: Nil). Taxes on profits assessable in the The People's Republic of China (the "PRC") have been calculated at the prevailing rates, based on existing legislation, interpretations and practices in respect thereof.

| | (Unaudited) Six months ended 30 June 2008 RMB'000 | (Unaudited) Six months ended 30 June 2007 RMB'000 |
|---|---|---|
| Current tax - Mainland China | | |
| Charge for the period | 42,310 | 10,303 |

According to the then income tax law of the PRC for foreign invested enterprises and foreign enterprises and as approved by relevant PRC tax authorities, Xtep (China) Co., Ltd. ("Xtep China"), a foreign-invested enterprise and wholly-owned subsidiary of the Group was entitled to a 50% reduction in the PRC enterprise income tax of the tax rate of 24% for the period ended 30 June 2007. Sanxing Sports Goods Co., Ltd. Quanzhou ("Sanxing Sports"), a wholly-owned subsidiary of the Group, was subject to the tax rate of 24% for the period ended 30 June 2007.

Under the new Enterprise Income Tax Law of the PRC ("New Tax Law") and its implementation rules (effective on 1 January 2008), the PRC enterprise income tax rate for domestic-invested and foreign-invested enterprises is unified to 25%. Also, a foreign-invested enterprise established before the New Tax Law was promulgated, which is entitled to foreign-invested enterprise income tax holiday, can continue to enjoy the existing tax holiday until its expiry subject to a 5-year period restriction.

Xtep (China) continues to enjoy the 50% reduction in the new unified PRC enterprise income tax rate of 25% for the years ending 31 December 2008 and 2009. Koling (Fujian) Garment Co., Ltd. ("Koling (Fujian)") enjoys exemption from the PRC enterprise income tax for the years ending 31 December 2008 and 2009 and thereafter will be entitled to a 50% reduction in the PRC enterprise income tax for the subsequent three years. Sanxing Sports is subject to the applicable tax rate for 25% with effect from 1 January 2008.

No provision for the PRC enterprise income tax has been made for other PRC companies comprising the Group for the six months ended 30 June 2008 (six months ended 30 June 2007: Nil) as they have not yet commenced business operations.

A reconciliation of the tax expense applicable to profit before tax using the applicable statutory rates for the jurisdictions in which the Company and the majority of its subsidiaries are operated to the tax expense at the effective tax rates are as follows:

| | (Unaudited) Six months ended 30 June 2008 RMB'000 | (Unaudited) Six months ended 30 June 2007 RMB'000 |
|---|---|---|
| Profit before tax | 296,974 | 91,380 |
| Tax at the applicable rates | 75,253 | 24,673 |
| Lower tax rate due to tax holidays | (36,062) | (15,670) |
| Expenses not deductible for tax | 1,160 | – |
| Tax losses not recognised | 1,959 | 1,300 |
| Tax charge at the Group's effective rate | 42,310 | 10,303 |

## 9. INTERIM DIVIDEND

| | (Unaudited) Six months ended 30 June 2008 RMB'000 | (Unaudited) Six months ended 30 June 2007 RMB'000 |
|---|---|---|
| Interim dividend – RMB4.4 cents (six months ended 30 June 2007: Nil) per ordinary share | 96,767 | – |

Note:

At a board meeting held on 1 September 2008, the board of directors declared and approved an interim dividend of HK5 cents (equivalent to RMB4.4 cents) per ordinary share, totalling HK$110,000,000 (equivalent to approximately RMB96,767,000), for the six months ended 30 June 2008.

## 10. EARNINGS PER SHARE ATTRIBUTABLE TO EQUITY HOLDERS OF THE COMPANY

### (a) Basic earnings per share

The calculation of basic earnings per share amount for the six months ended 30 June 2008 was based on the profit attributable to equity Shareholders of the Company for the period of RMB254,664,000 (six months ended 30 June 2007: RMB81,077,000 ) and the weighted average number of ordinary shares in issue during the six months ended 30 June 2008 of 1,590,383,811 (six months ended 30 June 2007: 1,468,500,007), as adjusted to reflect the conversion of Preferred Shares, capitalisation issues and the share offering during the period.

### (b) Diluted earnings per share

The calculation of diluted earnings per share amount for the six months ended 30 June 2008 is based on the profit attributable to the equity holders of the Company of RMB254,664,000 adjusted to reflect the imputed interest expense on preferred shares of RMB239,000 and the fair value gain on derivative component of preferred shares of RMB1,156,000. The weighted average number of ordinary shares of 1,734,615,384 used in the calculation is the weighted average number of ordinary shares in issue at 30 June 2008 as used in the basic earnings per share amounts calculation, and the weighted average number of ordinary shares assumed to have been issued at no consideration on the deemed conversion of 12,359,550 preferred shares and the corresponding 169,140,443 ordinary shares to be issued pursuant to the capitalisation issue. The Pre-IPO Share Options (as defined in note 24) outstanding during the period had anti-dilutive effect on the basic earnings per share amount for the period.

The calculation of the diluted earnings per share amount for the six months ended 30 June 2007 is based on the profit attributable to equity holders of the Company of RMB81,077,000. The weighted average number of ordinary shares of the Company of 1,471,781,773 used in the calculation is the weighted average number of ordinary shares of 1,468,500,007, as used in the basic earnings per share calculation, and the weighted average number of ordinary shares assumed to have been issued at no consideration on the deemed conversion of the convertible bonds into 2,247,190 ordinary shares and the corresponding 30,752,795 ordinary shares to be issued pursuant to the capitalisation issue.

## 11. DEPOSIT PAID

The deposit was paid for land use right over a parcel of land in Jinjiang, Fujian Province, the PRC. On 25 January 2008, a sales and purchase agreement was entered into between the Group and 泉州市通力模具有限公司 (Quanzhou Tongli Moulding Co., Ltd.*), an independent third party, for the transfer of the right arising from the aforesaid deposit paid at a consideration of RMB10,000,000. The consideration of RMB10,000,000 was fully paid by 泉州市通力模具有限公司 (Quanzhou Tongli Moulding Co., Ltd.*) to the Group in March 2008.

* For identification only

*30 June 2008*

## 12. INVENTORIES

| | (Unaudited) 30 June 2008 RMB'000 | (Audited) 31 December 2007 RMB'000 |
|---|---|---|
| Raw materials | 162,094 | 77,777 |
| Work in progress | 41,919 | 28,853 |
| Finished goods | 168,508 | 86,875 |
| | 372,521 | 193,505 |

## 13. TRADE AND BILLS RECEIVABLES

The trading terms with its customers are mainly on credit. The credit period is generally for a period of two to three months to its customers. An aged analysis of the trade receivables is as follows:

| | (Unaudited) 30 June 2008 RMB'000 | (Audited) 31 December 2007 RMB'000 |
|---|---|---|
| Within 90 days | 475,263 | 100,546 |
| 91 to 180 days | 9,303 | 67,861 |
| 181 to 360 days | 493 | 19,049 |
| Over 360 days | – | 1,129 |
| Trade receivables | 485,059 | 188,585 |
| Bills receivables | – | 45,798 |
| Trade and bills receivables | 485,059 | 234,383 |

The carrying amounts of trade and bills receivables approximate to their fair values.

*30 June 2008*

## 14. PREPAYMENTS, DEPOSITS AND OTHER RECEIVABLES

| | (Unaudited) 30 June 2008 RMB'000 | (Audited) 31 December 2007 RMB'000 |
|---|---|---|
| Prepayments | 24,193 | 49,512 |
| Deposits | 34,174 | 81,167 |
| Other receivables | 3,292 | 1,305 |
| | 61,659 | 131,984 |

## 15. FINANCIAL ASSETS AT FAIR VALUE THROUGH PROFIT OR LOSS

| | (Unaudited) 30 June 2008 RMB'000 | (Audited) 31 December 2007 RMB'000 |
|---|---|---|
| Money market fund outside Hong Kong, at fair value | 175,912 | – |
| | 175,912 | – |

## 16. CASH AND CASH EQUIVALENTS

| | (Unaudited) 30 June 2008 RMB'000 | (Audited) 31 December 2007 RMB'000 |
|---|---|---|
| Time deposits | 1,362,201 | – |
| Cash and bank balances | 749,242 | 215,018 |
| | 2,111,443 | 215,018 |
| Less: Pledged bank balances for bills payable | (5,400) | – |
| Cash and cash equivalents | 2,106,043 | 215,018 |

The cash and bank balances of the Group denominated in RMB amounted to approximately RMB717,681,000 as at 30 June 2008 (31 December 2007: RMB207,867,000). The RMB is not freely convertible into other currencies, however, under Mainland China's Foreign Exchange Control Regulations and Administration of Settlement, Sale and Payment of Foreign Exchange Regulations, the Group is permitted to exchange RMB for other currencies through banks authorised to conduct foreign exchange business.

Cash at banks earns interest at floating rates based on daily bank deposit rates. Short term time deposits are made for varying periods of between one month to three months depending on the immediate cash requirement of the Group, and earn interest at the respective short term deposit rates. The bank balances are deposited with creditworthy banks with no recent history of default. The carrying amounts of cash and bank balances approximate to their fair values.

## 17. TRADE AND BILLS PAYABLES

An aged analysis of the trade payables is as follows:

| | (Unaudited) 30 June 2008 RMB'000 | (Audited) 31 December 2007 RMB'000 |
|---|---|---|
| Within 90 days | 170,506 | 54,413 |
| 91 to 180 days | 163,670 | 1,179 |
| 181 to 360 days | 824 | 263 |
| Over 360 days | – | 4 |
| Trade payables | 335,000 | 55,859 |
| Bills payables | 27,000 | – |
| Trade and bills payables | 362,000 | 55,859 |

The trade payables are non-interest-bearing and are normally settled on 60 to 90-day terms. The carrying amounts of trade and bills payables approximate to their fair values.

## 18. DEPOSITS RECEIVED, OTHER PAYABLES AND ACCRUALS

| | (Unaudited) 30 June 2008 RMB'000 | (Audited) 31 December 2007 RMB'000 |
|---|---|---|
| Deposits received | 8,356 | 23,121 |
| VAT and other payables | 44,866 | 2,022 |
| Accruals | 35,351 | 15,959 |
| | 88,573 | 41,102 |

## 19. INTEREST-BEARING BANK BORROWINGS

| | (Unaudited) 30 June 2008 RMB'000 | (Audited) 31 December 2007 RMB'000 |
|---|---|---|
| Current: | | |
| Bank loans – secured | 223,000 | 101,000 |
| Bank loans – unsecured | 20,000 | 15,000 |
| | 243,000 | 116,000 |
| Analysed into: | | |
| Bank loans repayable within one year | 243,000 | 116,000 |

The above bank loans were all denominated in RMB. The bank loans bore fixed interest rates ranging from 6.318% to 7.470% per annum for the six months ended 30 June 2008 (Six months ended 30 June 2007: 5.508% to 6.561% per annum). Because of the short maturity, the carrying amounts of current bank loans approximate to their fair values.

The bank loans of RMB223,000,000 as at 30 June 2008 and RMB101,000,000 as at 31 December 2007 were secured by:

(i) corporate guarantees from Sanxing Sports and Koling (Fujian); and

(ii) mortgages over certain buildings and land use rights of the Group situated in Mainland China.

## 20. AMOUNT DUE TO A DIRECTOR

The amount due to a director was unsecured, interest-free and was repayable on demand. The Group had fully repaid the amount to the director before the Listing.

## 21. CONVERTIBLE BONDS AND PREFERRED SHARES

Carlyle Asia Growth Partners III, L.P. and Carlyle Asia Growth Partners III Co-Investment, L.P. (collectively the "Carlyle Investment Funds") entered into a series of convertible loan agreements, investment agreement and two supplemental agreements with the Group (collectively the "Agreements") on 13 June 2007, 24 August 2007 and 17 September 2007, respectively. Pursuant to the Agreements, the Carlyle Investment Funds agreed to subscribe the convertible bonds and preferred shares of the Company at a total consideration of approximately RMB220,000,000 and was injected into the Group by two tranches.

On 13 June 2007, the Carlyle Investment Funds made its first tranche of investment to the Company through the subscription of convertible bonds with principal amount of approximately RMB40,000,000 (the "Convertible Bonds"). The Convertible Bonds bear interest at 5% per annum and have a term of 6 months. On the maturity date, the Carlyle Investment Funds could request for the repayment or convert all or part of the Convertible Bonds into the Company's preferred shares at a valuation predetermined in the Agreements.

On 18 September 2007, the Carlyle Investment Funds made its second tranche of investment by subscribing 10,112,360 preferred shares of the Company (the "Preferred Shares") at a consideration of approximately RMB180,000,000. In addition, the Carlyle Investment Funds converted the Convertible Bonds into 2,247,190 Preferred Shares of the Company. In aggregate, the Carlyle Investment Funds held 12,359,550 Preferred Shares as at 18 September 2007, being the issuance date, and as at 31 December 2007.

Details of the terms of the Preferred Shares are set out in the Prospectus.

Details of the net proceeds received from the issue of the Convertible Bonds and Preferred Shares are analysed as follows:

| Convertible Bonds | RMB'000 |
|---|---|
| Nominal value of the Convertible Bonds issued on 13 June 2007 | 40,000 |
| Converted into 2,247,190 Preferred Shares | (40,000) |
| At 31 December 2007 | – |

| Preferred Shares | Notes | RMB'000 |
|---|---|---|
| Nominal value of 2,247,190 Preferred Shares issued upon the conversion of the Convertible Bonds | | 40,000 |
| Nominal value of 10,112,360 Preferred Shares issued during the period | | 180,000 |
| Transaction costs related to the liability component | | (2,256) |
| Derivative component at the issuance date | | (1,351) |
| Liability component at the issuance date | | 216,393 |
| Imputed interest expense for the period | | 206 |
| Liability component at 31 December 2007 | | 216,599 |
| Imputed interest expense for the period | | 239 |
| Conversion of Preferred Shares on 21 March 2008 | (a) | (27,447) |
| Conversion of Preferred Shares on 3 June 2008 | (b) | (189,391) |
| Liability component at 30 June 2008 | | – |
| Derivative component at the issuance date | | 1,351 |
| Fair value adjustment | | (27) |
| Derivative component at 31 December 2007 | | 1,324 |
| Conversion of Preferred Shares on 21 March 2008 | (a) | (168) |
| Fair value adjustment | | (1,156) |
| Derivative component at 30 June 2008 | | – |

Notes:

(a) On 21 March 2008, Carlyle Investment Funds converted a total of 1,565,168 Preferred Shares into 1,565,168 ordinary shares of the Company. These ordinary shares were then transferred to Group Success Investment Limited, a company owned by Ding Shui Po and Ding Mei Qing, who are considered as the controlling Shareholders of the Company, at a consideration of US$1. After the conversion, the Carlyle Investment Funds hold a total of 10,794,382 Preferred Shares.

(b) On 7 May 2008, the Carlyle Investment Funds exercised the conversion rights to the effect that conditional upon satisfaction of the conditions to the Company as set out in Appendix VI to the Prospectus, the remaining 10,794,382 Preferred Share would be converted into 10,794,382 ordinary shares of the Company. The pre-conditions for the conversion were fulfilled on the Listing Date and all the Preferred Shares were converted into the ordinary shares of the Company accordingly.

## 22. SHARE CAPITAL

The share capital as at 30 June 2008 and 31 December 2007 represented the issued capital of the Company and a summary of the authorised and issued share capital of the Company is as follows:

| At 30 June 2008 | HK'000 | RMB'000 |
|---|---|---|
| Authorised: | | |
| 100,000,000,000 ordinary shares of HK$0.01 each | 1,000,000 | 935,629 |
| Issued and fully paid: | | |
| 2,200,000,000 ordinary shares of HK$0.01 each | 22,000 | 19,409 |

| At 31 December 2007 | HK'000 | RMB'000 |
|---|---|---|
| Authorised: | | |
| 99,987,640,450 ordinary shares of HK$0.01 each | 999,876 | 935,513 |
| 12,359,550 Preferred Shares of HK$0.01 each | 124 | 116 |
| | 1,000,000 | 935,629 |
| Issued and fully paid: | | |
| 100,000,000 ordinary shares of HK$0.01 each | 1,000 | 936 |

A summary of the transactions from 10 April 2007 (date of incorporation) to 30 June 2008 with reference to below movements in the Company's authorised and issued ordinary and preferred shares capital is as follows:

### (a) Authorised share capital

| | Notes | Number of ordinary share of HK$0.01 each | Nominal value of ordinary shares HK$'000 | Nominal value of ordinary shares RMB'000 |
|---|---|---|---|---|
| *Authorised ordinary shares* | | | | |
| Upon incorporation | (i) | 38,000,000 | 380 | 356 |
| Increase during the period | (ii) | 99,949,640,450 | 999,496 | 935,157 |
| At 31 December 2007 and 1 January 2008 | | 99,987,640,450 | 999,876 | 935,513 |
| Redesignated as ordinary shares | (iii) | 12,359,550 | 124 | 116 |
| At 30 June 2008 | | 100,000,000,000 | 1,000,000 | 935,629 |

| | Notes | Number of Preferred Share of HK$0.01 each | Nominal value of Preferred Shares HK$'000 | Nominal value of Preferred Shares RMB'000 |
|---|---|---|---|---|
| *Authorised Preferred Shares* | | | | |
| Increase during the period | (ii) | 12,359,550 | 124 | 116 |
| At 31 December 2007 and 1 January 2008 | | 12,359,550 | 124 | 116 |
| Redesignated as ordinary shares | (iii) | (12,359,550) | (124) | (116) |
| At 30 June 2008 | | – | – | – |
| *Total authorised shares* | | | | |
| At 30 June 2008 | | 100,000,000,000 | 1,000,000 | 935,629 |
| At 31 December 2007 | | 100,000,000,000 | 1,000,000 | 935,629 |

Notes:

(i) The Company was incorporated in the Cayman Islands on 10 April 2007 with an authorised share capital of HK$380,000 divided into 38,000,000 ordinary shares of HK$0.01 each.

(ii) Pursuant to written resolutions of the sole shareholder of the Company passed on 17 September 2007, the authorised share capital of the Company was increased from HK$380,000 to HK$1,000,000,000 by the creation of an additional 99,949,640,450 ordinary shares of HK$0.01 each and 12,359,550 Preferred Shares ranking pari passu in all respects with the existing shares.

(iii) Pursuant to special resolutions of the Shareholders of the Company passed on 9 April 2008 and 7 May 2008, an aggregate of 12,359,550 Preferred Shares of HK$0.01 par value each were redesignated as ordinary shares of the Company of HK$0.01 each.

### (b) Issued ordinary shares

| | Notes | Number of ordinary share of HK$0.01 each | Nominal value of ordinary shares HK$'000 | Nominal value of ordinary shares RMB'000 |
|---|---|---|---|---|
| Issued: | | | | |
| Upon incorporation | | | | |
| – issued nil paid | (i) | 1 | – | – |
| Allotment of shares | | | | |
| – on 27 June 2007 | (ii) | 99 | – | – |
| – on 17 September 2007 | (iii) | 99,999,900 | 1,000 | 936 |
| At 31 December 2007 and 1 January 2008 | | 100,000,000 | 1,000 | 936 |
| Issued pursuant to conversion of Preferred Shares | | | | |
| – on 21 March 2008 | (iv) | 1,565,168 | 16 | 14 |
| – on 3 June 2008 | (v) | 10,794,382 | 108 | 95 |
| Capitalisation issue credited as fully paid conditional on the share premium account of the Company, being credited as a result of the issue of the new shares to the public | (vi) | 1,537,640,450 | 15,376 | 13,526 |
| New issue of shares | (vii) | 550,000,000 | 5,500 | 4,838 |
| At 30 June 2008 | | 2,200,000,000 | 22,000 | 19,409 |

Notes:

(i) On 10 April 2007, one ordinary share of the Company was allotted and issued at par as nil paid to the initial subscriber and was immediately transferred to Ding Shui Po. On 28 May 2007, Group Success Investments Limited ("Group Success"), a company incorporated in the BVI and is beneficially owned by Ding Shui Po, acquired the one ordinary share of the Company from Ding Shui Po.

(ii) On 27 June 2007, an additional 99 ordinary shares of the Company were allotted at par and credited as nil paid to Group Success.

(iii) On 17 September 2007, an additional 99,999,900 ordinary shares of the Company were allotted at par and credited as fully paid to Group Success.

(iv) On 21 March 2008, the Carlyle Investment Funds converted a total of 1,565,168 Preferred Shares into 1,565,168 ordinary shares of the Company. The conversion resulted in an increase in share capital and share premium account by HK$16,000 (equivalent to approximately RMB14,000) and HK$28,478,000 (equivalent to approximately RMB27,601,000), respectively.

(v) On 3 June 2008, the Carlyle Investment Funds converted the remaining 10,794,382 Preferred Shares into 10,794,382 ordinary shares of the Company. The conversion resulted in an increase in share capital and share premium account by HK$108,000 (equivalent to approximately RMB95,000) and HK$195,255,000 (equivalent to approximately RMB189,296,000), respectively.

(vi) Pursuant to a resolution passed on 7 May 2008, a total of 1,537,640,450 new ordinary shares of HK$0.01 each were further allotted and issued, credited as fully paid at par by the Company, by way of capitalisation of the sum of HK$15,376,000 (equivalent to approximately RMB13,526,000) from the share premium account, to the then existing Shareholders of the Company, whose names appeared on the register of the Company on 3 June 2008, in proportion to their respective shareholdings. Such allotment and capitalisation were conditional on the share premium account being credited as a result of the issue of new ordinary shares to the public in connection with the Company's initial public offering ("IPO") as detailed in (vii) below.

(vii) In connection with the Company's IPO, 550,000,000 shares of HK$0.01 each were issued at a price of HK$4.05 per share for a total cash consideration, before related issuance expenses, of HK$2,227,500,000 (equivalent to approximately RMB1,959,531,000). Dealings in these shares on the Stock Exchange commenced on 3 June 2008.

## 23. RESERVES

The amounts of the Group's reserves and movement therein for the six months ended 30 June 2008 are presented in the condensed consolidated statement of changes in equity.

The capital reserve represents the excess of the nominal value of the paid-in capital of the subsidiaries acquired pursuant to the Group Reorganisation over the consideration paid for acquiring these subsidiaries.

In accordance with the relevant regulations applicable in the PRC, subsidiaries established in the PRC are required to transfer a certain percentage of their statutory annual profits after tax (after offsetting any prior year's losses), if any, to the statutory surplus fund until the balance of the fund reaches 50% of their respective registered capital. Subject to certain restrictions as set out in the relevant PRC regulations, the statutory surplus fund may be used to offset against accumulated losses of the respective PRC subsidiaries. The amount of the transfer is subject to the approval of the board of directors of the respective PRC subsidiaries.

## 24. PRE-IPO SHARE OPTION SCHEME

### (a) Pre-IPO share option scheme

The Company has adopted a pre-IPO share option scheme on 7 May 2008 (the "Pre-IPO Scheme") for the purpose of giving the Group's employees an opportunity to have a personal stake in the Company and help motivate the Group's employees to optimise their performance and efficiency, and also to retain the Group's employees whose contributions are important to the long-term growth and profitability of our Group.

The principal terms of the Pre-IPO Scheme, approved by written resolutions of the Company's Shareholders and the Carlyle Investment Funds passed on 7 May 2008, are as follows:

(a) the subscription price per share under the Pre-IPO Scheme shall be at a 20% discount to the offer price of the Company's shares in the IPO;

(b) the total number of shares which may be issued upon the exercise of all options granted under the Pre-IPO Scheme is 19,000,000;

(c) all options granted under the Pre-IPO Scheme can only be exercised in the following manner:

| *Exercise period* | *Maximum percentage of options exercisable* |
|---|---|
| Anytime after the first anniversary of the Listing Date | 30% of the total number of options granted |
| Anytime after the second anniversary of the Listing Date | 30% of the total number of options granted |
| Anytime after the third anniversary of the Listing Date | 40% of the total number of options granted |

(d) each option granted under the Pre-IPO Share Option Scheme has a 10-year exercise period.

(e) share options issued under the Pre-IPO Scheme do not confer rights on the holders to dividends or to vote at Shareholders' meetings.

On 7 May 2008, an aggregate of 19,000,000 share options (the "Pre-IPO Share Options") under the Pre-IPO Scheme were issued to a director of the Company and certain employees of the Group. The exercise prices and exercise periods of the Pre-IPO Share Options outstanding at 30 June 2008 are as follows:

| *Number of options* | *Exercise per share* | *Exercise period* |
|---|---|---|
| 5,700,000 | HK$3.24* | 3 June 2009 to 2 June 2019 |
| 5,700,000 | HK$3.24* | 3 June 2010 to 2 June 2020 |
| 7,600,000 | HK$3.24* | 3 June 2011 to 2 June 2021 |
| 19,000,000 | | |

* The exercise price of the Pre-IPO Share Options equals to a 20% discount to the offer price of HK$4.05 of the Company's ordinary shares in the IPO.

The fair value of the Pre-IPO Share Options granted during the period was estimated at RMB11,051,000, of which the Company recognised a share option expense of RMB921,000 during the six months ended 30 June 2008.

The fair value of the Pre-IPO Share Options granted during the period was estimated as at the date of grant by Norton Appraisals Limited, an independent firm of professionally qualified valuers, using the Black-Scholes-Merton Option Pricing Model, taking into account the terms and conditions upon which the options were granted. The following table lists the inputs to the model used:

| | |
|---|---|
| Exercise price (HK$ per share) | 3.24 |
| Expected dividend yield (%) | 2.0 |
| Expected volatility (%) | 39.8 |
| Risk-free interest rate (%) | 2.143 |
| Expected life of share options (years) | 3.08 |
| Weighted average share price at grant date (HK$) | 2.73 |

The expected life of the Pre-IPO Share Options is not necessarily indicative of the exercise patterns that may occur. The expected volatility may not necessarily reflect the actual outcome.

No other feature of the options granted was incorporated into the measurement of fair value.

At 30 June 2008, the Company had outstanding Pre-IPO Share Options for the subscription of 19,000,000 shares under the Pre-IPO Share Option Scheme. The exercise in full of the Pre-IPO Share Options would, under the present capital structure of the Company, result in the issue of 19,000,000 additional ordinary shares of the Company and additional share capital of HK$190,000 and share premium account of HK$61,370,000 (before issue expenses).

At the date of approval of the Condensed Consolidated Interim Financial Statements, the Company had 19,000,000 Pre-IPO Share Options outstanding under the Pre-IPO Share Option Scheme, which represented approximately 0.9% of the issued share capital of the Company as at that date.

**(b) Share option Scheme**

The Company has also adopted a share option scheme ("the Share Option Scheme") pursuant to the Shareholders' written resolution passed on 7 May 2008.

The maximum number of shares that may be granted under the Share Option Scheme and other share option schemes shall not exceed 30% of the number of issued shares of the Company from time to time. No option may be granted to any person such that the total number of shares of the Company issued and to be issued upon exercise of all options granted and to be granted to each participant in any 12-month period up to the date of the latest grant exceeds 1% of the number of shares of the Company in issue.

An option under the Share Option Scheme may be exercised in accordance with the terms of the Scheme at any time during a period as determined by the Board of Director of the Company, which must not be more than 10 years from the date of the grant.

No share option has been granted under the Share Option Scheme during the period.

## 25. COMMITMENTS

(a) The commitments as at the end of each period are as follows:

| | (Unaudited) 30 June 2008 RMB'000 | (Audited) 31 December 2007 RMB'000 |
|---|---|---|
| Contracted for commitment in respect of its wholly-foreign-owned investments in the PRC | 89,264 | 7,952 |
| Contracted for commitment in respect of: | | |
| – construction of new buildings | 2,393 | 67 |
| – acquisition of land use rights | – | 4,667 |
| – advertising and promotional expenses | 125,389 | 41,820 |
| | 217,046 | 54,506 |

(b) For the period from 1 November 2006 to 31 December 2009 (subject to satisfaction of certain conditions, it could be extended to 31 December 2012), the Group is obliged to pay a minimum guaranteed royalty to a licensor, however, such amount will be adjusted based on the actual sales amount of the product for these years.

## 26. OPERATING LEASE ARRANGEMENTS

As at 30 June 2008, the Group had total future minimum lease payments under non-cancellable operating leases falling due as follows:

| | (Unaudited) 30 June 2008 RMB'000 | (Audited) 31 December 2007 RMB'000 |
|---|---|---|
| Within one year | 1,760 | 1,703 |
| In the second to fifth years, inclusive | 3,367 | 5,062 |
| | 5,127 | 6,765 |

## 27. APPROVAL OF THE INTERIM FINANCIAL STATEMENTS

The unaudited interim financial statements were approved and authorised for issue by the board of directors on 1 September 2008.

# Report on Review of Interim Financial Statements

安 永

**To the Shareholders of Xtep International Holdings Limited**
*(Incorporated in the Cayman Islands with limited liability)*

## Introduction

We have reviewed the interim financial statements of Xtep International Holdings Limited set out on pages 33 to 58 which comprises the condensed consolidated balance sheet as at 30 June 2008, and the condensed consolidated income statement, the condensed consolidated statement of changes in equity and the condensed consolidated cash flow statement for the six-month period then ended and other explanatory notes. The Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited require the preparation of a report on interim financial information to be in compliance with the relevant provisions thereof and Hong Kong Accounting Standard 34 "Interim Financial Reporting" ("HKAS 34") issued by the Hong Kong Institute of Certified Public Accountants.

The directors are responsible for the preparation and fair presentation of these interim financial statements in accordance with HKAS 34. Our responsibility is to express a conclusion on these interim financial statements based on our review. Our report is made solely to you, as a body, in accordance with our agreed terms of engagement, and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report.

## Scope of review

We conducted our review in accordance with Hong Kong Standard on Review Engagements 2410 "Review of Interim Financial Information Performed by the Independent Auditor of the Entity" issued by the Hong Kong Institute of Certified Public Accountants. A review of interim financial report consists of making inquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with Hong Kong Standards on Auditing and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

## Conclusion

Based on our review, nothing has come to our attention that causes us to believe that the interim financial statements do not present fairly, in all material respects, in accordance with HKAS 34.

**Ernst & Young**
*Certified Public Accountants*

18/F, Two International Finance Centre
8 Finance Street, Central
Hong Kong

1 September 2008

# Glossary

In this interim report, unless the content states otherwise, the following expressions have the following meanings:

| | |
|---|---|
| "Board" | the board of Directors |
| "BVI" | the British Virgin Islands |
| "CAGR" | compounded annual growth rate |
| "Company" | Xtep International Holdings Limited (特步國際控股有限公司), an exempted company incorporated with limited liability under the laws of the Cayman Islands on 10 April 2007 |
| "Corporate Governance Code" | the code provisions contained in the Code on Corporate Governance Practices |
| "Director(s)" | the director(s) of the Company |
| "Euromonitor International" | Euromonitor International (Asia) Pte Ltd, an Independent Third Party, which engages in the provision of international market intelligence on consumer products, services and lifestyles |
| "Group" | the Company and its subsidiaries |
| "Group Success" | Group Success Investments Limited (群成投資有限公司), a company incorporated in the BVI with limited liability on 23 February 2007, the entire issued capital of which is directly owned as to 63.2% by Mr. Ding Shui Po and 36.8% by Ms. Ding Mei Qing |
| "Hong Kong" | the Hong Kong Special Administrative Region of the PRC |
| "HK$" | Hong Kong Dollars, the lawful currency of Hong Kong |
| "Hong Kong Stock Exchange" | the Stock Exchange of Hong Kong Limited |
| "Listing" | the Listing of the Shares on the main board of the Hong Kong Stock Exchange |
| "Listing Rules" | the Rules Governing the Listing of Securities on the Hong Kong Stock Exchange |
| "Model Code" | Model Code for Securities Transaction by Directors of Listed Issuers |
| "OEM" | acronym for original equipment manufacturer, a business that manufactures goods or equipment for branding and resale by others |
| "PRC" or "China" | the People's Republic of China |
| "RMB" | Renminbi, the lawful currency of the PRC |
| "Share(s)" | ordinary share(s) of HK0.10 each in the share capital of the Company |
| "Shareholders" | Shareholders of the Company |
| "SFO" | the Securities and Future Ordinance |