



RAINBOW INTERNATIONAL HOLDINGS LIMITED

彩虹國際控股有限公司

(Incorporated in the Cayman Islands with limited liability)

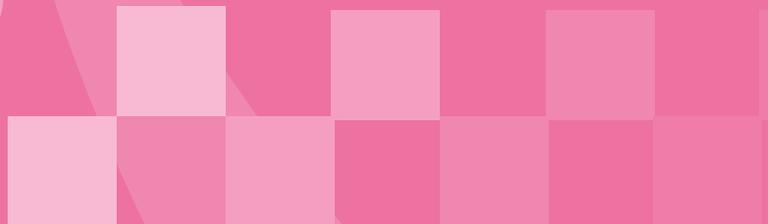
2001 Annual Report



Annual Report



2001



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This document, for which the directors (the "Directors") of Rainbow International Holdings Limited (the "Company") collectively and individually accept responsibility, includes particulars given in compliance with the Rules Governing the Listing of Securities on the Growth Enterprise Market of The Stock Exchange of Hong Kong Limited (the "GEM Listing Rules") for the purpose of giving information with regard to the Company. The Directors, having made all reasonable enquiries, confirm that, to the best of their knowledge and belief: (1) the information contained in this document is accurate and complete in all material respects and not misleading; (2) there are no other matters the omission of which would make any statement in this document misleading; and (3) all opinions expressed in this document, have been arrived at after due and careful consideration and are founded on bases and assumptions that are fair and reasonable.

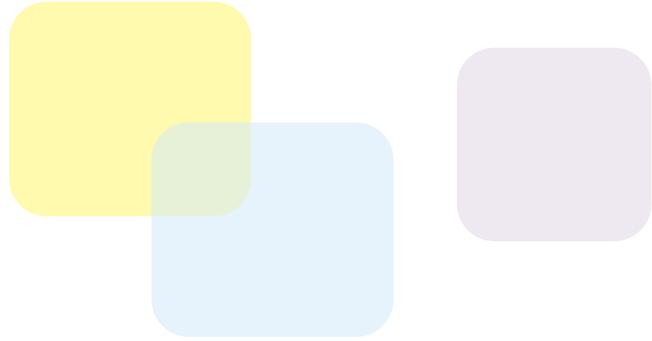
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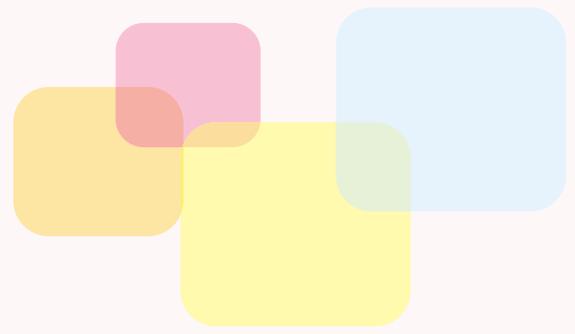
CORPORATE PROFILE

Rainbow International Holdings Limited (the "Company") and its subsidiaries (collectively, the "Rainbow Group") is principally engaged in retail and wholesale of branded beauty products in Hong Kong. The beauty products sold by Rainbow Group may be broadly divided into three main categories, namely (i) skin-care products, (ii) fragrances and cosmetics and (iii) hair-care and personal care products and accessories.

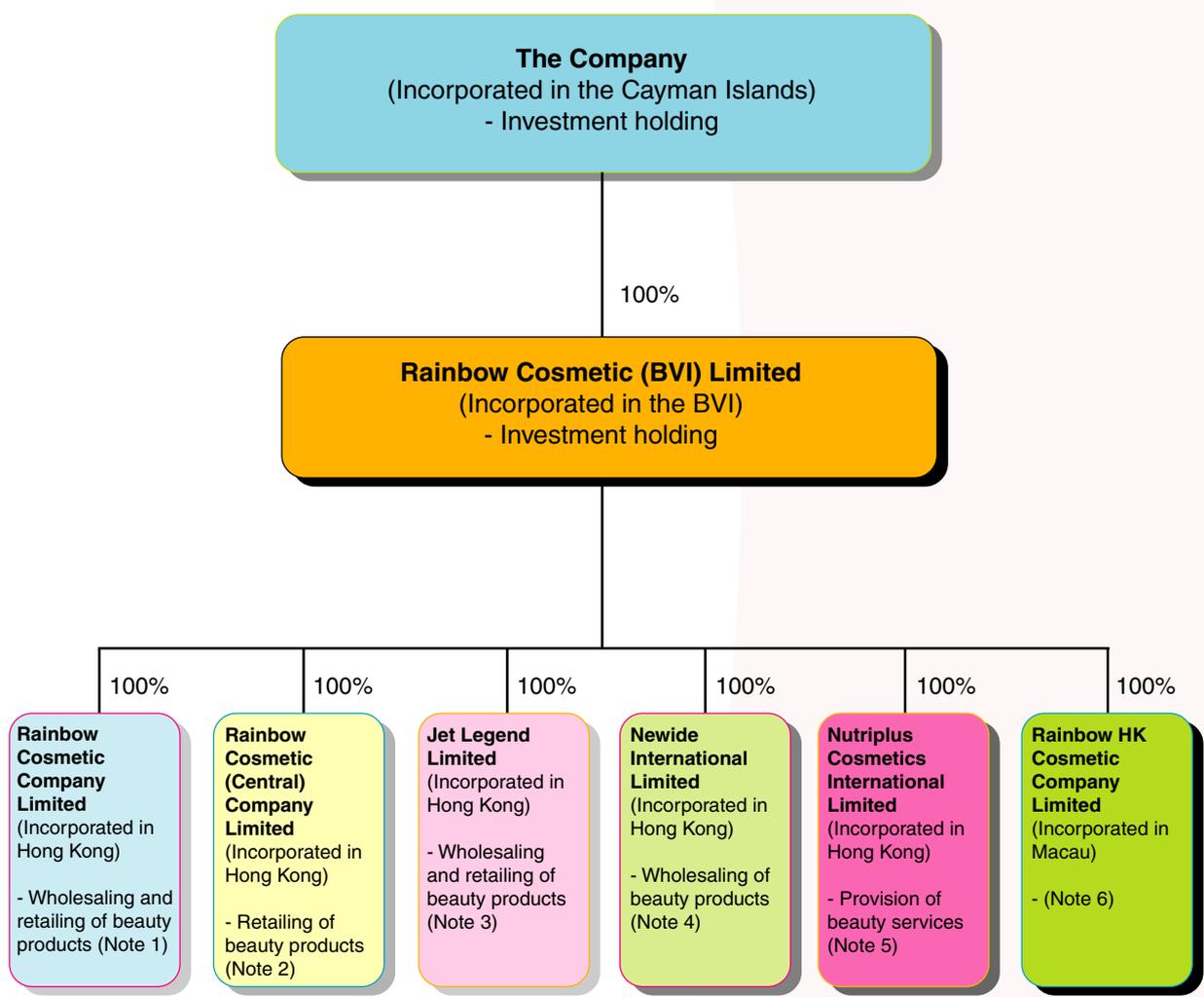
On 15 October 2001, the Company was successfully listed on GEM, its ordinary shares are traded under the stock code 8079. The successful listing of the Company represented a milestone in the development of Rainbow Group.

Currently, Rainbow Group has eight retail outlets under its trade name of Rainbow Cosmetics and three beauty centres under the trade name of Nutriplus in different prime locations in Hong Kong.





The following is the organisation structure of Rainbow Group



Notes:

1. Rainbow Cosmetic Company Limited operates two Rainbow Cosmetic outlets in Causeway Bay and three Rainbow Cosmetic outlets in Mongkok. Rainbow Cosmetic also engages in the wholesale business at the Rainbow Cosmetic outlets operated by it.
2. Rainbow Cosmetic (Central) Company Limited operates one Rainbow Cosmetic outlet in Central.
3. Jet Legend Limited operates one Rainbow Cosmetic outlet in Tsimshatsui and one Rainbow Cosmetic outlet in Admiralty. Jet Legend also engages in the wholesale business at the Rainbow Cosmetic outlets operated by it.
4. Newide International Limited engages in the wholesale business.
5. Nutriplus Cosmetics International Limited operates three beauty centres in Mongkok, Causeway Bay and Central.
6. Rainbow HK Cosmetic Company Limited did not carry on any business.

Corporate information

Directors

Executive Directors

LI Ngar Kwan, Aldy - Chairperson
LIANG Kwong Lim - Deputy Chairman
Elbert LEE
CHAN Sin Kwan

Non-executive Director

LAI Tin Ying, Michael (alias LAI Siu Tin)

Independent non-executive Directors and members of audit committee of the board of Directors

TAM Fung Chee
CHIU Wai

Company secretary

LO Yu Wah FCCA, AHKSA

Compliance officer

Elbert LEE

Qualified accountant

LO Yu Wah FCCA, AHKSA

Legal advisers on Hong Kong law

Sit, Fung, Kwong & Shum

Legal advisers on the Cayman Islands law

Maples and Calder Asia

Sponsor

DBS Asia Capital Limited

Auditors

Charles Chan, Ip & Fung CPA Ltd.
Certified Public Accountants
37th Floor, Hennessy Centre
500 Hennessy Road
Causeway Bay
Hong Kong

Principal share registrar and transfer office

Bank of Butterfield International (Cayman) Ltd.
P.O. Box 705
Butterfield House
Fort Street, George Town
Grand Cayman
Cayman Islands
British West Indies

Hong Kong branch share registrar and transfer office

Standard Registrars Limited
5th Floor, Wing On Centre
111 Connaught Road Central
Hong Kong

Registered office

Ugland House
P.O. Box 309
George Town
Grand Cayman
Cayman Islands
British West Indies

Head office and principal place of business in Hong Kong

4th Floor, Flat B
Sze Hing Loong Ind. Bldg.
44 Lee Chung Street
Chai Wan
Hong Kong

Principal bankers

Chekiang First Bank Ltd.
123 Cheung Sha Wan Road
Kowloon
Hong Kong

Hang Seng Bank Limited
83 Des Voeux Road Central
Hong Kong

Shanghai Commercial Bank Ltd.
18 Pennington Street
Hong Kong

The Hongkong and Shanghai Banking Corp. Ltd.
673 Nathan Road
Kowloon
Hong Kong

Website

www.i-rainbow.com.hk

Stock Code

8079

Chairperson's Statement

Highlights

- Successfully listed on GEM on 15 October 2001
- Turnover for the financial year ended 31 October 2001 was approximately HK\$110,047,000, representing a decrease of approximately 12.77%, as compared with the previous financial year
- Loss for the financial year ended 31 October 2001 was approximately HK\$25,803,000
- As at 31 October 2001, Rainbow International Holdings Limited and its subsidiaries had approximately HK\$29.1 million in cash and bank balance with HK\$38.8 million of debt
- The board of directors of the Company (the "Board") does not recommend the payment of a dividend



Business Review

On behalf of the Board, I am pleased to present the first annual results for the year ended 31 October 2001, which follows our successful listing on GEM on 15 October 2001.

Rainbow Group is principally engaged in the retail and wholesale of branded beauty products while also providing a comprehensive range of dedicated beauty care treatment services in Hong Kong. The products may be broadly divided into three main categories; namely (i) skin care products, (ii) fragrance and cosmetics and (iii) hair-care and personal-care products and accessories. Rainbow Group is committed to maintaining a high quality of the products and beauty services provided and, the establishment of beauty centres under the trade name of Nutriplus is an extension of this precept.





The net proceeds raised from the initial listing of the shares of the Company on GEM on 15 October 2001 were approximately HK\$21 million. The net proceeds have been applied to achieve business objectives as set out in the prospectus and detailed below:

For the period from 15 to 31 October 2001

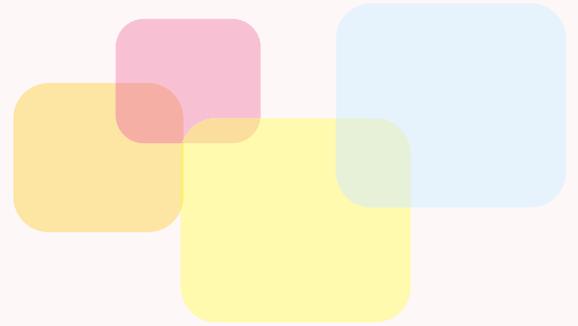
	As stated in Prospectus up to 31 October 2001 HK\$million	Actual HK\$million	
To repay certain bank loans of Rainbow Group	8.00	4.10	<i>Note 1</i>
To conduct extensive advertising and marketing programmes and other corporate image enhancement programmes	0.30	–	<i>Note 2</i>
To implement and enhance the management information system of Rainbow Group	<u>0.75</u>	<u>–</u>	<i>Note 3</i>
	<u><u>9.05</u></u>	<u><u>4.10</u></u>	

Note 1: Seeing the sluggish economy of Hong Kong, the Board considered that it is in the best interest of the Rainbow Group to maintain a higher level of working capital, therefore the remaining outstanding bank loans are rearranged and would be repaid completely within two years by instalments.

Note 2: Resources utilised for advertising and promotion activities were concentrated on December 2001.

Note 3: The Board is studying different solutions to implement and enhance the management information system which would be more cost-effective. The Board believes the whole process would be completed in the first half year of calendar year 2002.

Amidst the sluggish economic climate in Hong Kong, which is a result of the global economic downturn, which affects the Hong Kong retail market, the performance of Rainbow Group for the financial year ended 31 October, 2001 was adversely affected. Nevertheless, the Board is confident that, with the anticipated modest recovery of the Hong Kong economy in 2002 and the improvement of various sales promotion strategies, particulars of which are described below further, Rainbow Group will be able to capture additional business opportunities and its performance is expected to improve with anticipated modest recovery of Hong Kong economy.



The Board will continue to pursue the business objectives of Rainbow Group as stated in the Prospectus. The Board will use additional efforts towards positioning Rainbow Group as one of the leading beauty products and services providers in Hong Kong. With the anticipated recovery of the Hong Kong economy, together with our strong management team, the Board believes that Rainbow Group will be able to meet the challenges ahead and will become one of the leading beauty products and services providers in Hong Kong.

As at 31 October 2001, Rainbow Group had eight retail outlets under its trade name of Rainbow Cosmetic and three beauty centres under the trade name of Nutriplus in prime business locations in Hong Kong.

On behalf of the Board, I would like to express our appreciation for the continuing support of our shareholders and the invaluable contributions made by management and staff.

Ms. LI Ngar Kwan, Aldy

Chairperson

Hong Kong, 25 January 2002



Management discussion and analysis



Operations in Review

Year 2000/2001 marked a milestone period in the development of Rainbow Group. The successful listing of the shares of the Company on 15 October 2001 signified a major stride forward in our corporate status and provided additional impetus for our business development. The last twelve months also saw Rainbow Group maintaining a policy of expansion, accommodating changes and making improvements with a view towards achieving sustainable growth. As we believe that women will always seek ways to present a better personal image and thus place greater emphasis on quality beauty products and services, this provides a driving force for our business growth. With the effective execution of our business and investment strategies, we believe that Rainbow Group is well-established in the beauty product and service identity ahead of our competitors.

Nevertheless, the business of Rainbow Group and, in particular, its retail business, resembles all other retail businesses in Hong Kong and is subject to general economic condition of Hong Kong economy, the level of domestic consumption and the number of tourist coming to Hong Kong and their aggregate spending in Hong Kong. The attack at the World Trade Centre in New York, the US, on 11 September 2001 is believed to have directly and indirectly influenced the global economy. It is also expected that further short-term growth of global economy may be slowed down as a result of the incident. Thus, the overall Hong Kong economy has been adversely affected and this also has been reflected in the performance and profitability of Rainbow Group for the financial year ended 31 October 2001.



Products

The last financial year represented a significant time for Rainbow Group as we introduced a new and exclusive range of beauty products under the trade name of Nutriplus. In May 2001, Rainbow Group first launched 11 skin-care products and eight hair-care products under this brand name, targeting customers aged 25 and above. Following which, Rainbow Group subsequently engaged the services of a specialist firm in Switzerland to develop and manufacture a series of 11 skin-care products. Building on this business development programme, Rainbow Group then sought the expertise of a local beauty product agent in the production of a series of eight hair-care products. To strengthen brand loyalty of Nutriplus, a beauty centre called Nutriplus has been established which offers beauty treatment with Nutriplus skin-care products. In addition to the Nutriplus brand, Rainbow Group has also obtained the exclusive distribution rights for the Helvance and Bicosmetic skin care beauty brands. The Directors are confident that the launch of these new and exclusive series of beauty products will strengthen the corporate image of the Rainbow Group and reinforce brand recognition by consumers.

Retail Outlets under the Trade Name of Rainbow Cosmetic

For the financial year ended 31 October 2001, sales generated by Rainbow Cosmetic outlets accounted for approximately 69.36% of turnover as compared with 76.19% for the previous year and recorded sales of HK\$76.3 million, signifying a decline of 20.58% or HK\$19.8 million over the previous year. As the pavement outside certain Rainbow Cosmetic outlets are under construction, it has caused adverse effect to these outlets. Also, competition since August 2001 has been particularly keen. Rainbow Cosmetic outlets had to follow the price competition within the industry. Thus, turnover of Rainbow Cosmetic outlets has decreased for the financial year ended 31 October 2001. Nevertheless, the Rainbow Cosmetic outlets that are ideally located in prime business locations with high pedestrian traffic in Hong Kong will be able to facilitate the growth of Rainbow Group's business in this highly competitive retail environment.

Beauty Services Business under the Trade Name of Nutriplus

The turnover generated from the provision of beauty services by Rainbow Group increased to 5.90% of total turnover for the financial year ended 31 October 2001 due to the launch of Nutriplus skin-care treatment. To broaden this customer base and satisfy customers' needs, Rainbow Group now owns three beauty centres that are located in Mongkok, Causeway Bay, and Central, respectively, enjoying high levels of pedestrian traffic and maximum visibility.

As at 31 October 2001, Rainbow Group employed 19 beauticians, 6 of whom obtained diplomas, certificates, and/or equivalent accreditation from recognised institutes while all have an average of three years experience in the beauty service industry. To complement this highly competent workforce, and to provide complete quality care, Rainbow Group also plans to invest in the latest beauty-care equipment and technology. The Directors are confident that from such initiatives, Rainbow Group will build on a solid reputation for excellence and expand on its beauty service business.

Wholesale Business

Rainbow Group also engages in the wholesale of certain branded beauty products. Among the customers of this segment of Rainbow Group's business are wholesale agents and distributors. For the period under review, Rainbow Group recorded sales of HK\$27.2 million which represented 24.74% of total turnover for the financial year ended 31 October 2001 or a decline of 3.21% over the previous financial year. The Directors are optimistic that the wholesale business will grow once the economy recovers.





Sales, Marketing, and Promotions

Establishing a well respected brand image is important for the growing business of Rainbow Group. As part of Rainbow Group's growth strategy to become a leading provider of beauty products and services in Hong Kong, a marketing team comprising four members has been established. Already, in a campaign to increase public awareness, Rainbow Group regularly utilises such channels as magazines, newspaper, television, and radio to promote its corporate image. For the period under review, Rainbow Group expended nearly HK\$1.5 million on advertising, representing approximately 3% of selling and distribution expenses of Rainbow Group for the financial year ended 31 October 2001.

In order to promote customer loyalty and stimulate purchases at Rainbow Cosmetic outlets, a free membership programme was launched in 1999. As at 31 October 2001, Rainbow Group had approximately 13,000 holders of the Rainbow membership card. Information and catalogues on beauty products available at the Rainbow Cosmetic outlets are provided to cardholders of this card and thus, they are constantly informed of the latest beauty products as well as any special promotional items. Cardholders may also enjoy a discount of five percent on all items (including discounted items) purchased at Rainbow Cosmetic outlets.

www.i-rainbow.com.hk

Representative of Rainbow Group's customer loyalty enhancement strategy, Rainbow Group's website www.i-rainbow.com.hk was launched in Hong Kong in June 2001 providing up-to-date online information on special or new beauty products and services offered by Rainbow Group.



Overseas Expansion

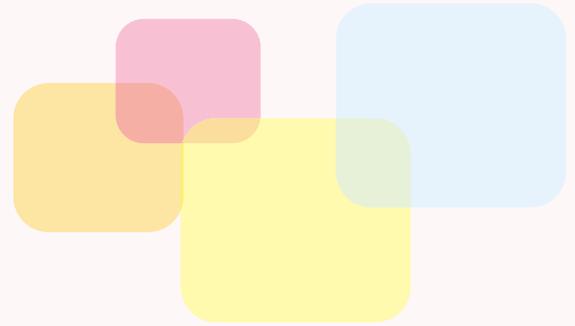
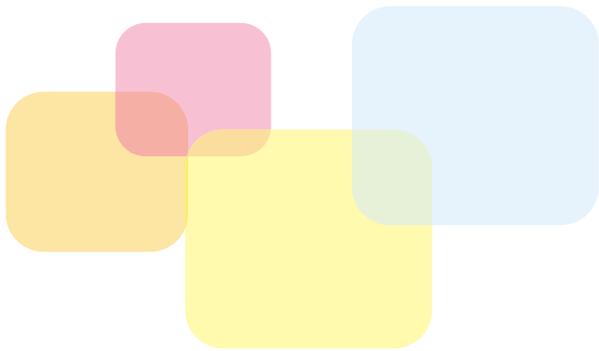
Consistent with a goal to branch out towards different Chinese communities, Rainbow Group has recently leased property in Macau and will commence retail operations within the first half of calendar year 2002. With China's accession into the World Trade Organization and the winning of the bid to host the 2008 Olympic Games by Beijing, the Directors anticipate that the People's Republic of China (the "PRC") government will gradually abolish the import tariffs on, inter alia, imported beauty products. This is expected to stimulate the demand for imported beauty products particularly in certain major PRC cities, such as Shanghai, Beijing and Guangzhou, and may provide additional business opportunities to Rainbow Group.

Financial Review

During the year ended 31 October 2001, Rainbow Group achieved a turnover of approximately HK\$110 million, a decrease of 12.77% over the corresponding period of 31 October 2000. Loss attributable to shareholders amounted to approximately HK\$25.8 million. The Directors do not recommend the payment of a dividend.

As Rainbow Group was undergoing a period of development and investment during the period under review, an increase in manpower costs and associated fixed assets were incurred, hence a net loss of approximately HK\$25.8 million was recorded. Rainbow Group will continue to review the performance of each Rainbow Cosmetic outlet and may not renew the leases in respect of its retail outlets located at 58 Sai Yeung Choi Street South, Mongkok and 518 Lockhart Road, Causeway Bay upon their expiry in February and March 2002 respectively. The Directors believe that the closing of these two Rainbow Cosmetic outlets is beneficial to the improvement of the operating results of Rainbow Group. We therefore remain optimistic of Rainbow Group's growth in the coming years.

Having successfully listed the Company's shares on the GEM, Rainbow Group obtained net proceeds of approximately HK\$21 million. As at 31 October 2001, the cash and bank balance of Rainbow Group amounted to approximately HK\$29.1 million.



Financial Position

As at 31 October 2001, Rainbow Group had total assets of approximately HK\$80.9 million (2000: HK\$69.0 million), including cash and bank balances of approximately HK\$29.1 million (2000: HK\$0.1 million). Approximately HK\$12.1 million (2000: Nil) of such cash and balances were pledged to secure banking facilities. Bank overdrafts, trust receipt loans and bank loans as at 31 October 2001 was approximately HK\$20.5 million, HK\$13.4 million and HK\$4.9 million respectively. All the bank borrowings are secured by the aforesaid cash deposits, units of trust fund of approximately HK\$8.5 million, corporate guarantee executed by the Company and one of the Company's subsidiaries of approximately HK\$19 million, legal charges on certain properties and units of trust fund held by, and the fixed deposits maintained in the name of Ms. Li Ngar Kwan, Aldy, fixed deposits maintained in the name of an individual connected with Ms. Li Ngar Kwan, Aldy. As at 31 October 2001, Rainbow Group's total available banking facilities was approximately HK\$38.4 million of which approximately HK\$33.6 million was utilised. Unutilised banking facilities was therefore of approximately HK\$4.8 million. Up to the date of this report, certain fixed deposits and units of trust fund in the name of Ms. Li Ngar Kwan, Aldy secured for the banking facilities of Rainbow Group has been released. The release of the other securities in the name of Ms. Li Ngar Kwan, Aldy and the individual connected with her is still in progress pending the relevant bank's review of the results of Rainbow Group for the year ended 31 October 2001. It is currently expected that such release would be completed by end of March 2002.

The Directors believe that following the recovery of the economy from the short-term adverse effect by the incident of 911, Rainbow Group would generate funds sufficient to meet its ongoing operating and development requirements.

The gearing ratio (total debts/net assets) of Rainbow Group as at 31 October 2001 was 308% (2000: N/A).

Since most of the transactions of Rainbow Group are denominated in Hong Kong dollars, no hedging or other arrangements to reduce the currency risk have been implemented.



Contingent Liabilities

As of the date of this report, the Directors are not aware of any material contingent liabilities.

Employees

As at 31 October 2001, Rainbow Group had 130 (2000: 111) full-time employees. The total of employee remuneration, including that of the Directors, for the year ended 31 October 2001 amounted to approximately HK\$21.2 million (2000: HK\$16.2 million). Rainbow Group remunerates its employees based on their performance, experience and the prevailing industry practice.

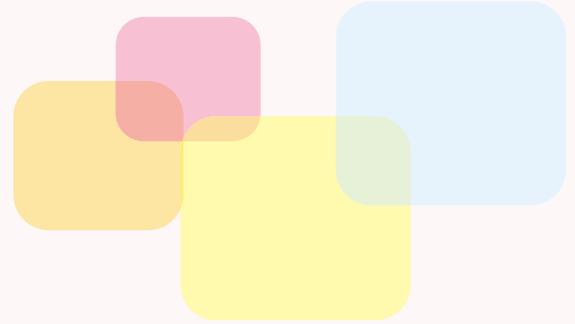
Share Option Schemes

On 24 September 2001, two share option schemes of the Company were approved by shareholders of the Company, namely, the Pre-IPO Share Option Scheme and the Share Option Scheme (both terms as defined in the Prospectus). The summary of the terms of the two schemes has been set out in Appendix IV of the Prospectus under the section headed "Share Option Schemes".

As at 31 October 2001, the Company had granted 35,000,000 options under the Pre-IPO Share Option Scheme, of which four executive Directors and one non-executive Director was granted options to subscribe for an aggregate of 15,575,000 shares at an exercise price of HK\$0.25 each. As at 31 October 2001, no options were granted under the Share Option Scheme.

Future Plans and Prospects

It is Rainbow Group's intention to expand operations both in terms of scale and scope of business in order to achieve rapid growth. Moreover, Rainbow Group aims to become a leading beauty products and services provider in Hong Kong. In order to realise such objectives, the following plans will be undertaken:



Expand Retail Operations

To expand on the retail segment of the business, the Directors will continue to open new Rainbow Cosmetic outlets in prime Hong Kong locations.

Furthermore, with gradual improvements in Macau's economy, the Directors also foresees growing demand for beauty products in that region, where competition is relatively less intense. In capitalising on such an opportunity, the Directors have established a Rainbow Cosmetic outlet in Macau for which operations will commence within the first half of calendar year 2002.

Focus on the Provision of Comprehensive Beauty Services

Recognising the increasing demand for complete beauty care, the Directors will continue to set up specialised beauty centres in Hong Kong under the Nutriplus trade name and provide such comprehensive services as facials, body treatments, and hair-care for both women and men. Likewise, the Directors will allocate resources for investing in advanced beauty-care equipment and technology. Additional equipment that are expected to be acquired include Isopei for skin treatment (專業修身美體機), Bio R-2000 for treating muscle and face lines (智能數碼美療儀器), Cellu M6 for body toning (纖體健膚儀器), Aesthi Peel for treating pigments, wrinkles, face lines, as well as acne scars and marks (金鋼磨砂皮膚更生儀器), Linfopei for treating water retained in the body (淋巴導向去水腫排毒儀器), and Therapeutic for treating body fat (熱能振盪按摩理療艙).

Expand on the Wholesale Business of Rainbow Group

With China's accession into the World Trade Organization and the winning of the bid to host the 2008 Olympic Games by Beijing, it will offer much business opportunities to investors. The Directors also believe that continuous economic development and improvement in living standards in the PRC will give rise to an increasing demand for beauty products. To capitalise on such vast business potential, Rainbow Group intends to expand on its wholesale business in the PRC, subject to satisfactory feasibility studies.

Improve on the Quality of Services at Rainbow Cosmetic Outlets and Beauty Centres

The Directors understand that quality service is crucial for achieving success. To this end, Rainbow Group will implement a series of training programmes (including in-house training and joint training with suppliers) to improve the standard of services and product knowledge of sales representatives at Rainbow Cosmetic outlets.

Promote the Corporate Image and Strengthen Brand Loyalty of Nutriplus Products

To maintain a competitive advantage over competitors in the retail business segment the Directors believe that it is vital to cultivate strong brand loyalty and recognition of Rainbow Group. As such, the Directors intend to implement a series of initiatives including advertising campaigns, renovating Rainbow Cosmetic outlets and beauty centres, as well as participating in public functions to promote the corporate image of the Rainbow Group as a leading provider of beauty products and services. Additionally, Rainbow Group will also develop beauty products under the Nutriplus label as part of its brand enhancement programme.

Strengthen the Management Information System of the Rainbow Group

As at 31 October 2001, four out of the eight Rainbow Cosmetic outlets had implemented an integrated inventory control system. The Directors recognise the importance of implementing such a system at all Rainbow Cosmetic outlets so as to enable management to respond to changing market demands promptly and maintain an appropriate level and variety of inventory. Hence, the Directors intend to upgrade and enhance the existing inventory control systems by implementing a comprehensive electronic point-of-sales platform at all Rainbow Cosmetic outlets.



Comparison of business objectives with actual business progress

The following is a summary of the actual progress made in comparison with the business objectives that were set out in the Prospectus from the period of 28 September 2001 to 31 October 2001.

Business Objectives

Retail Expansion

- To identify potential locations in Hong Kong for expansion of Rainbow Cosmetic outlets
- To explore potential business opportunities in the retail market for beauty products in Macau

Marketing and Promotions

- To promote Nutriplus beauty products through a series of marketing and promotion campaigns
- To generate maximum visibility for Nutriplus beauty products through the distribution of free samples
- To promote Rainbow Group's corporate image in Hong Kong through advertisements on billboards and television as well as in magazines and newspapers

Actual Business Progress

- To facilitate continuous business growth, Tsuen Wan or the New Territories are considered as potential locations for expansion of Rainbow Cosmetic outlets in calendar year 2002.
- Rainbow Group has established a Rainbow Cosmetic outlet in Macau in November 2001 for which operations will commence within the first half of calendar year 2002.
- Rainbow Group started to promote since December 2001 the Nutriplus line of products by placing advertisements in magazines that targets females aged between 25-45. Additionally, the employment of a public relation agency and exposure through news reporting will be utilised.
- The distribution of free samples to our customers through Rainbow Cosmetic outlets, and special offers to VIP members, including free treatments at Nutriplus Beauty Salons has been implemented since December 2001.
- The Rainbow Group purchased airtime on ATV as well as placing product advertisements in local newspapers in December 2001 as part of the efforts to promote its corporate image.

Human Resources

- To recruit additional staff, to complete the implementation of a bar-code-reading inventory control systems at all Rainbow Cosmetic outlets, and to continue in the development of an integrated management information system that incorporates an electronic point-of-sales platform
- To recruit additional sales representatives with expertise in the beauty product industry
- To continue in the implementation of training seminars (including in-house training and joint training programmes with suppliers) for existing and new sales representatives and beauticians while also educating them on the latest industry trends
- Rainbow Group is in the process of recruiting additional staff and is in the process of completing the bar-code system. It is expected that the bar-code system will be completed within the first half of calendar year 2002. Presently preparing a strategy to increase the efficiency of Rainbow Group's inventory control system
- Currently, no additional sales representative has been recruited as it is not considered necessary under current market condition
- In-house and on-the-job training programmes have been implemented for existing staff in order to keep them abreast of industry trends and new product introductions

THREE YEARS FINANCIAL SUMMARY

	2001 <i>HK\$'000</i>	2000 <i>HK\$'000</i>	1999 <i>HK\$'000</i>
Turnover	<u>110,047</u>	<u>126,157</u>	<u>128,887</u>
Profit/(loss) attributable to shareholders	<u>(25,803)</u>	<u>2,165</u>	<u>(14,256)</u>

Notes:

- (1) The Company was incorporated in the Cayman Islands on 6 March 2001 and became the holding company of Rainbow Group with effect from 21 September 2001 as a result of the Group Reorganisation as set out in the Prospectus. Accordingly, the only consolidated balance sheets prepared by Rainbow Group are those set out on page 35.
- (2) The results of Rainbow Group for each of two years ended 31 October 2000 have been extracted from the Company's Prospectus dated 28 September 2001.
- (3) The result for the year ended 31 October 2001 have been extracted from the consolidated income statement as set out on page 34.
- (4) The financial summary of Rainbow Group has been prepared on the combined basis as if the group structure had be in existence throughout the years concerned. Refer to Note 1 to the accompanying financial statements for details of the Reorganisation.

DIRECTORS AND SENIOR MANAGEMENT OF RAINBOW GROUP

DIRECTORS

Executive Directors

Ms. LI Ngar Kwan, Aldy, aged 45, is the chairperson of Rainbow Group since its establishment in 1985. Ms. Li Ngar Kwan, Aldy is also the founder of Rainbow Group and an executive Director and is responsible for the overall strategic planning and business development of Rainbow Group. Ms. Li Ngar Kwan, Aldy has in-depth knowledge and extensive experience in beauty product retail and wholesale businesses in Hong Kong. Prior to establishment of Rainbow Group, Ms. Li Ngar Kwan, Aldy had approximately 15 years of experience in beauty product retail business in Hong Kong.

Mr. LIANG Kwong Lim, aged 60, is an executive Director responsible for the sales and marketing functions of Rainbow Group. Prior to joining Rainbow Group in January 2001, Mr. Liang has approximately 30 years of experience in export and import trade businesses.

Mr. Elbert LEE, aged 28, is an executive Director responsible for the purchasing function of Rainbow Group and also responsible for the wholesale business of Rainbow Group. Mr. Elbert Lee is also the Compliance Officer of the Company for the purpose of the GEM Listing Rules. Mr. Elbert Lee graduated from the University of Toronto with a Bachelor Degree of Applied Science and Engineering. Mr. Elbert Lee joined Rainbow Group as purchasing manager in June 1997. Mr. Elbert Lee is a nephew of Ms. Li Ngar Kwan, Aldy.

Ms. CHAN Sin Kwan, aged 39, is an executive Director responsible for the retail business development of the *Rainbow Cosmetic* outlet at Admiralty Centre, Central, Hong Kong. Ms. Chan is also responsible for the overall administration and business operations of all Rainbow Cosmetic outlets. Prior to joining Rainbow Group in May 1989, Ms. Chan has approximately 12 years of experience in Hong Kong jewellery and cosmetics retail businesses.

Non-executive Director

Mr. LAI Tin Ying, Michael (alias LAI Siu Tin), aged 54, is a non-executive Director responsible for public relations of Rainbow Group and other promotion and marketing activities of Rainbow Group. Prior to joining Rainbow Group in June 2001, Mr. Lai has approximately 20 years of experience in public relation and media industry.

Independent non-executive Directors

Ms. TAM Fung Chee, aged 40, was appointed as an independent non-executive Director in June 2001. Ms. Tam is also an associate member of Hong Kong Society of Accountants and a fellow member of Chartered Association of Certified Accountants. Ms. Tam has approximately 20 years of experience in accounting and finance industry.

Mr. CHIU Wai, aged 69, was appointed as an independent non-executive Director in June 2001. Mr. Chiu is currently a director of Lai Sun Garment (International) Limited, the shares of which are listed on the Main Board. Mr. Chiu has approximately 40 years of experience in garment manufacturing industry.

DIRECTORS AND SENIOR MANAGEMENT OF RAINBOW GROUP

SENIOR MANAGEMENT

Mr. LO Yu Wah, aged 37, is the financial controller and the Qualified Accountant of the Company and the Company Secretary of the Company. Mr. Lo is responsible for the overall financial and accounting functions of Rainbow Group. Prior to joining Rainbow Group in May 2001, Mr. Lo acted as financial controller of a listed company for approximately five years. Mr. Lo is an associate member of Hong Kong Society of Accountants and a fellow member of Association of Chartered Certified Accountants in the United Kingdom.

Ms. PANG Ka Ping, Veronica, aged 45, is the chief operation officer of Rainbow Group and is responsible for the overall retail operations, information technology development, logistics and general administration of Rainbow Group. Ms. Pang also oversees the enhancement of Rainbow Group's management information systems and inventory control systems and the business development of new series of beauty products, such as *Nutriplus*. Ms. Pang holds a Bachelor of Arts Degree from the University of Toronto, Canada. Prior to joining Rainbow Group in March 1996, Ms. Pang has approximately ten years of experience in retail business in Canada and approximately five years of experience in retail banking business in Hong Kong.

Mr. WU Chui Fan, aged 35, is the retail outlet supervisor of Rainbow Group and oversees, in particular, the retail operations for the two *Rainbow Cosmetic* outlets in Causeway Bay and the one in Central. Prior to joining Rainbow Group in November 1994, Mr. Wu has approximately ten years of experience in beauty product industry.

Ms. SAM Swee Lin, aged 36, is the retail outlet supervisor of Rainbow Group and oversees, in particular, the retail operations for the two *Rainbow Cosmetic* outlets in Mongkok and the one in Tsimshatsui. Prior to joining Rainbow Group in June 1994, Ms. Sam has approximately ten years of experience in beauty product industry.

Ms. CHEUNG Lin Heung, aged 31, is the retail outlet supervisor of Rainbow Group and oversees the retail operations for one *Rainbow Cosmetic* outlet in Mongkok. Prior to joining Rainbow Group in April 1996, Ms. Cheung has approximately eight years of experience in beauty product industry.

REPORT OF THE DIRECTORS

The directors of the Company (“Directors”) present their annual report together with the audited financial statements of the Company and Rainbow Group for the year ended 31 October 2001.

REORGANISATION AND LISTING ON THE GROWTH ENTERPRISE MARKET

The Company was incorporated in the Cayman Islands on 6 March 2001 as an exempted company with limited liability under the Companies Law (Revised) of the Cayman Islands. Pursuant to a reorganisation of Rainbow Group in preparation for the listing of the Company’s shares on the Growth Enterprise Market (“GEM”) of The Stock Exchange of Hong Kong Limited (the “Stock Exchange”), the Company became the holding company of Rainbow Group. The Company’s shares were listed on the GEM on 15 October 2001.

PRINCIPAL ACTIVITIES

The Company is an investment holding company. Rainbow Group is principally engaged in the retails and wholesales of beauty products in Hong Kong. The beauty products sold by Rainbow Group include (i) skin-care products, (ii) fragrances and cosmetics and (iii) hair-care and personal-care products and accessories.

An analysis of Rainbow Group's turnover and contribution to (loss)/profit before taxation by principal activity for each of the two years ended 31 October 2001 is as follows:

	2001		2000	
	(Loss) before		Profit before	
	Turnover	taxation	Turnover	taxation
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Retails and wholesales of beauty products	103,558	(25,689)*	124,240	2,162*
Beauty services	6,489	(114)	1,917	398
	<u>110,047</u>	<u>(25,803)</u>	<u>126,157</u>	<u>2,560</u>

No geographical analysis of Rainbow Group’s turnover and their respective contribution to (loss)/profit before taxation is presented as all the turnover is attributable to business conducted in Hong Kong.

* The result of beauty services generated from turnover of approximately HK\$523,000 (2000 : approximately HK\$1,244,000) has been included.

REPORT OF THE DIRECTORS

MAJOR CUSTOMERS AND SUPPLIERS

The percentages of purchases and sales attributable to Rainbow Group's major suppliers and customers are as follows:–

	2001 %	2000 %
Purchases		
– the largest supplier	13.31	66.72
– five largest suppliers combined	29.65	73.08

Sales to Rainbow Group's five largest customers accounted for less than 30% of Rainbow Group's turnover for each of the two years ended 31 October 2001.

The largest supplier of Rainbow Group was Rainbow Trading Company ("Rainbow Trading") which was wholly owned by Mr. Elbert Lee. Of the purchases from Rainbow Trading for the year ended 31 October 2000 and the two months ended 31 December 2000, approximately 13.83% and 12.80% respectively, was attributable to the purchases of Rainbow Trading from a company in Canada which is wholly owned by a brother of Ms. Li Ngar Kwan, Aldy. Rainbow Trading was acquired by Newide International Limited, a wholly-owned subsidiary of the Company, as part of the reorganisation of Rainbow Group and the acquisition was completed after the close of business on 31 December 2000.

Save as disclosed above, none of the directors or any of their associates (as defined in the Rules Governing the Listing of Securities on GEM ("GEM Listing Rules")) or any shareholders of the Company (who, to the knowledge of the Directors, own more than 5% of the issued share capital of the Company) had any beneficial interest in any of the five largest suppliers or customers of Rainbow Group for the financial year ended 31 October 2001.

RESULTS AND APPROPRIATIONS

The results of Rainbow Group for the year ended 31 October 2001 are set out in the consolidated income statement on page 34 of the annual report.

The Directors do not recommend the payment of a dividend.

FINANCIAL SUMMARY

A summary of the results and of the assets and liabilities of Rainbow Group for the last three years is set out on page 18.

FIXED ASSETS

Details of the movements in fixed assets of Rainbow Group are set out in note 9 to the financial statements.

REPORT OF THE DIRECTORS

ISSUED CAPITAL AND SHARE OPTIONS

Details of the movements in issued capital and share options of the Company during the year are set out in notes 20 and 23, respectively, to the financial statements.

RESERVES

Movements in reserves during the year are set out in note 21 to the financial statements.

DONATIONS

During the year, charitable and other donations of approximately HK\$38,000 (2000: HK\$15,500) were made.

SUBSIDIARIES

Particulars of the Company's subsidiaries are set out in note 10 to the financial statements.

DIRECTORS

The Directors who held office during the year are:

Executive directors

Mapcal Limited	(appointed on 6 March 2001 and resigned on 6 March 2001)
LI Ngar Kwan, Aldy	(appointed on 6 March 2001)
LIANG Kwong Lim	(appointed on 6 March 2001)
Elbert LEE	(appointed on 6 March 2001)
CHAN Sin Kwan	(appointed on 11 June 2001)

Non-executive directors

LAI Tin Ying, Michael (alias LAI Siu Tin)	(appointed on 11 June 2001)
TAM Fung Chee**	(appointed on 11 June 2001)
CHIU Wai**	(appointed on 11 June 2001)

** *Independent Non-executive Directors*

In accordance with Article 116 of the Articles of Association of the Company, Mr. Liang Kwong Lim and Mr. Elbert Lee will retire and, being eligible, offer themselves for re-election at the forthcoming annual general meeting of the Company.

DIRECTORS' SERVICE CONTRACTS

Each of the executive Directors has entered into a continuous service contract with the Company on 24 September 2001 for an initial term of two years (in case of Mr. Liang Kwong Lim) or three years (in case of other executive Directors) commencing from 1 September 2001 and thereafter be continuous unless and until terminated by not less than six months' notice (in case of Ms. Li Ngar Kwan Aldy) or three months' notice (in case of each other executive Directors) in writing served by either party on the other.

REPORT OF THE DIRECTORS

DIRECTORS' SERVICE CONTRACTS (continued)

The non-executive Directors (including the independent non-executive Directors) have no fixed term of office but are subject to the provisions of retirement and rotation of Directors under the Articles of Association of the Company.

Save as disclosed above, none of the Directors being proposed for re-election at the forthcoming annual general meeting of the Company has entered into any service arrangements with any member of Rainbow Group (excluding contracts expiring or determinable by Rainbow Group within one year without payment of compensation other than statutory compensation).

DIRECTORS' INTEREST IN SECURITIES

As at 31 October 2001, the interests of the Directors and chief executives in the shares and options of the Company and its associated corporations (as defined in the Securities (Disclosure of Interests) Ordinance ("SDI Ordinance")) as recorded in the register maintained by the Company pursuant to section 29 of the SDI Ordinance or as required, pursuant to rules 5.40 to 5.59 of the GEM Listing Rules, to be notified to the Company and the Stock Exchange were as follows:

(a) shares of the Company

Name	Type of Interest	No. of Shares
Ms. Li Ngar Kwan, Aldy	Personal	181,552,291
Mr. Elbert Lee	Personal	5,231,897
Mr. Lai Tin Ying, Michael (alias Lai Siu Tin)	Personal	2,186,434
Mr. Chiu Wai	Personal	3,279,652

(b) share options

Ms. Li Ngar Kwan, Aldy, Mr. Liang Kwong Lim, Mr. Elbert Lee and Mr. Lai Tin Ying, Michael (alias Lai Siu Tin), being Directors of the Company, have been granted certain share options under the Pre-IPO Share Option Scheme. Details of such share options are set out in the paragraph headed "Share Option Schemes" herein below.

Save as disclosed herein above, as at 31 October 2001, none of the Directors or chief executive had any personal, family, corporate or other interests in the share capital of the Company or its associated corporations as recorded in the register maintained under section 29 of the SDI Ordinance or as required, pursuant to rules 5.40 to 5.59 of the GEM Listing Rules, to be notified to the Company and the Stock Exchange.

SHARE OPTION SCHEMES

On 24th September 2001, two share option schemes of the Company were conditionally approved by the shareholders of the Company, namely Pre-IPO Share Option Scheme and Share Option Scheme, both of which became unconditional on 14 October 2001.

REPORT OF THE DIRECTORS

SHARE OPTION SCHEMES (continued)

(A) Share Option Scheme

A summary of the purpose and certain principal terms of the Share Option Scheme is set out below. Further details of the terms of the Share Option Scheme have been set out in Appendix IV of the prospectus of the Company dated 28 September 2001 (the “Prospectus”).

(a) Purpose

The purpose of the Share Option Scheme is to provide incentive or recognize the contribution of the employees (whether full time or part time) and directors (whether executive, non-executive or independent non-executive directors) of the Company and/or its subsidiaries. The following is a summary of certain principal terms of the Share Option Scheme conditionally adopted by a resolution of the shareholders of the Company on 24 September 2001 (which became unconditional on 14 October 2001):—

(b) Who may join

The Board may, at its discretion, offer full-time or part time employees and executive, non-executive and independent non-executive directors of the Company and/or any of its subsidiaries, options to subscribe for such number of new Shares as the Board may determine at an exercise price determined in accordance with paragraph (d) below.

(c) Consideration payable upon grant

Upon acceptance of the option, the grantee shall pay HK\$1.00 to the Company by way of consideration for the grant.

(d) Price of Shares

The subscription price of a Share in respect of any particular option granted under the Share Option Scheme shall be such price notified by the Board to the grantee, being not less than the highest of (i) the closing price of the Shares on GEM as stated in the Stock Exchange’s daily quotation sheet on the date of offer of the option and (ii) the average of the closing prices of the Shares on GEM as stated in the Stock Exchange’s daily quotation sheets for the five days on which the Stock Exchange is open for the business of dealing in securities immediately preceding the date of offer of the option; and (iii) the nominal value of a Share. Where the Company has been listed for less than 5 business days, the Offer Price shall be used as the closing price for any business day falling within the period before listing of the Shares on GEM for the above purpose.

(e) Maximum number of Shares

- (i) Subject to the compliance of paragraphs (ii), (iii) and (iv) below, the total number of Shares which may be issued upon exercise of all outstanding options granted under the Share Option Scheme and any other share option schemes of the Company (including the Pre-IPO Share Option Scheme) and yet to be exercised at any time shall not, in aggregate, exceed 30 per cent. of the issued share capital of the Company from time to time, during a period of ten years from 24 September 2001 excluding for this purpose (aa) Shares issued and allotted or which may be issued or allotted pursuant to the exercise of options granted pursuant to the Share Option Scheme and any other share option schemes of the Company and (bb) any pro rata entitlements to further Shares issued in respect of those Shares mentioned in (aa) above.

REPORT OF THE DIRECTORS

SHARE OPTION SCHEMES (continued)

(A) Share Option Scheme (continued)

(e) Maximum number of Shares (continued)

- (ii) The total number of Shares which may be issued upon exercise of all options which may be granted under the Share Option Scheme and any other share option schemes of the Company (but excluding the options conditionally granted under the Pre-IPO Share Option Scheme in respect of 35,000,000 Shares) must not, in aggregate, exceed 10 per cent. of the issued share capital of the Company as at the date on which dealings of the Shares on GEM commence (the "Scheme Mandate Limit") unless shareholders' approval has been obtained pursuant to paragraph (iii) or (iv) below. Options lapsed in accordance with the terms of the Share Option Scheme or any other share option scheme of the Company under which such options are granted, as the case may be, shall not be counted for the purpose of calculating whether the Scheme Mandate Limit has been exceeded.
- (iii) Subject to paragraph (i) above, the Scheme Mandate Limit may be renewed by shareholders of the Company in general meeting from time to time provided that the Scheme Mandate Limit so renewed must not exceed ten (10) per cent. of the issued share capital of the Company at the date of the approval of the renewal by the shareholders of the Company. Upon any such renewal, all options granted under the Share Option Scheme and any other share option schemes of the Company (including those outstanding, cancelled, lapsed in accordance with the Share Option Scheme or any other share option scheme of the Company and exercised options) prior to the approval of such renewal shall not be counted for the purpose of calculating whether the renewed Scheme Mandate Limit has been exceeded. A circular must also be sent to the shareholders of the Company containing such information from time to time required by the Stock Exchange.
- (iv) Subject to paragraph (i) above, the Board may seek separate shareholders' approval in general meeting to grant options beyond the Scheme Mandate Limit provided that the options in excess of the Scheme Mandate Limit are granted only to the participants specified by the Board before such approval is sought and the Board must issue a circular to the shareholders of the Company containing such information from time to time required by the Stock Exchange in relation to any such proposed grant to specified participants.
- (v) No option may be granted to any one person which if exercised in full would result in the total number of Shares issued and to be issued upon exercise of the share options already granted or to be granted to him under the Share Option Scheme or any other share option scheme from time to time adopted by the Company (including both exercised and outstanding share options) in the 12-month period immediately preceding the date of such new grant exceeding 1 per cent. of the issued share capital of the Company as at the date of such new grant. Any grant of further share options above this limit shall be subject to the following requirements:–
 - (aa) approval of the shareholders of the Company at general meeting, with such proposed grantee abstaining from voting, having been obtained;
 - (bb) a circular in relation to the proposal for such further grant having been sent by the Company to its shareholders with such information from time to time required by the Stock Exchange;

REPORT OF THE DIRECTORS

SHARE OPTION SCHEMES (continued)

(A) Share Option Scheme (continued)

(e) Maximum number of Shares (continued)

(v) (continued)

(cc) the number and terms of the options to be granted to such proposed grantee shall be fixed before the shareholders' approval mentioned in sub-paragraph (aa) above; and

(dd) for the purpose of calculating the minimum subscription price for the Shares in respect of the further options proposed to be so granted as described under the heading "Price of Shares" above, the date of board meeting for proposing such grant of further options shall be taken as the date of offer of the option.

(f) Time of exercise of option

An option may be exercised in accordance with the terms of the Share Option Scheme at any time during a period ("Option Period") to be notified by the Board to each grantee, such period not to exceed 10 years from the date on which the option is offered in accordance with the terms of the Share Option Scheme.

There is no general requirement on the minimum period for which an option must be held or the performance targets which must be achieved before an option can be exercised under the terms of the Share Option Scheme. However, at the time of granting any option, the Board may make such grant subject to such terms and conditions in relation to the minimum period of the options to be held and/or the performance targets to be achieved as the Board may determine in its absolute discretion.

(g) Period of the Share Option Scheme

Subject to earlier termination by the Company in general meeting, the Share Option Scheme shall be valid and effective for a period of ten years from and including 24 September, 2001, the date on which the Share Option Scheme was conditionally adopted by the Company. After such ten years' period, options which are granted during the life of the Share Option Scheme and remain unexpired immediately prior to the end of the said ten years' period may continue to be exercisable in accordance with their terms of issue within three years after the end of such ten-year of period.

As at 31 October 2001, no option has been granted or agreed to be granted to any person under the Share Option Scheme.

(B) Pre-IPO Share Option Scheme

The purpose of the Pre-IPO Share Option Scheme is to recognise the contribution of certain directors, employees, consultants and advisers of Rainbow Group to the growth of Rainbow Group and/or to the listing of the Shares on GEM. The principal terms of the Pre-IPO Share Option Scheme are substantially the same as the terms of the Share Option Scheme except, among others, that:-

(a) the subscription price for each Share is HK\$0.25;

REPORT OF THE DIRECTORS

SHARE OPTION SCHEMES (continued)

(B) Pre-IPO Share Option Scheme (continued)

- (b) the aggregate number of Shares subject to the Pre-IPO Share Option Scheme is 35,000,000 equivalent to 10 per cent. of the enlarged issued share capital of the Company as at the date on which dealings of the Shares on GEM first commence;
- (c) the grantees eligible for the options include full-time employees of the Company and/or its subsidiaries and employees who are not in full-time employment of the Company and/or its subsidiaries including executive, non-executive and independent non-executive directors of the Company and/or its subsidiaries and any consultants and advisers to the Company and/or any of its subsidiaries;
- (d) no options shall be granted to any one person which will result in the total number of Shares issued and to be issued upon exercise of all the share options granted or to be granted to him under the Pre-IPO Share Option Scheme or any other share option scheme from time to time adopted by the Company exceeding one (1) per cent. of the enlarged issued share capital of the Company immediately after completion of the Capitalisation Issue and the Share Offer (each as defined in the Prospectus), assuming the Over-allotment Option (as defined in the Prospectus) is not exercised;
- (e) save for the options which have been conditionally granted under the Pre-IPO Share Option Scheme (see below), no further options will be offered or granted under the Pre-IPO Share Option Scheme, as the right to do so ended upon the date prior to the day on which the registration of this prospectus with the Registrar of Company in Hong Kong takes place, being 26 September 2001 (the "Expiry Date").

Further details of the Pre-IPO Share Option Scheme are set out at pages 247 and 248 of the Prospectus.

As at 31 October 2001, the Company had granted options to subscribe for an aggregate of 35,000,000 shares to (i) four executive Directors and one non-executive Director for an aggregate of 15,575,000 shares, (ii) International Capital Network Limited, being the financial adviser to the Company, for 3,500,000 shares and (iii) 43 full-time employees (including six senior management staff) of Rainbow Group for an aggregate of 15,925,000 shares. The particulars of the share options granted under the Pre-IPO Share Option Scheme are set out as follows:–

Name	Number of Share options	Date of grant	Exercise price per share (HK\$)
Li Ngar Kwan, Aldy*	3,500,000	24 September 2001	0.25
Liang Kwong Lim*	3,500,000	24 September 2001	0.25
Elbert Lee*	3,500,000	24 September 2001	0.25
Lai Tin Ying, Michael (alias Lai Siu Tin)**	3,500,000	24 September 2001	0.25
Chan Sin Kwan*	1,575,000	24 September 2001	0.25
International Capital Network Limited***	3,500,000	24 September 2001	0.25
Other 43 employees of Rainbow Group	15,925,000	24 September 2001	0.25

REPORT OF THE DIRECTORS

SHARE OPTION SCHEMES (continued)

(B) Pre-IPO Share Option Scheme (continued)

Notes:—

- * Being the Directors of the Company
- ** Being the Non-executive Director of the Company
- *** Being the financial adviser to the Company

All of the above share options have a duration of three years commencing from 15 October 2001, being the date on which dealings in the shares of the Company on GEM first commence, but each shall lapse in accordance with the terms of the Pre-IPO Share Option Scheme if the relevant grantee (other than International Capital Network Limited) ceases to be a director or an employee of Rainbow Group or on any other ground set forth in the Pre-IPO Share Option Scheme. Under the terms of the share options granted under the Pre-IPO Share Option Scheme, these share options (other than the share options granted to International Capital Network Limited) can only be exercised by the grantees in the following manner:—

Commencement date when the share option become exercisable (Note)

Proportion of the share options granted under the Pre-IPO Share Option Scheme that can be exercised

the date falling 6 months from the date on which dealings in the shares of the Company on GEM first commence	one-third
the first anniversary of the date on which dealings in the shares of the Company on GEM first commence	one-third
the second anniversary of the date on which dealings in the shares of the Company on GEM first commence	one-third

Note: Dealings of the shares of the Company first commenced on 15 October 2001.

No valuations of options granted under the Pre-IPO Share Option Scheme are included in this report as the Directors consider that, as the shares of the Company were only listed since 15 October 2001, there would not be sufficient historical price performance data to produce reasonable valuations using commonly used methodologies.

DIRECTORS' INTERESTS IN CONTRACTS

No contracts of significance in relation to the business of the Company or any of its subsidiaries was a party and in which any of the Company's Directors or members of its management had a material interest, either directly or indirectly, subsisted at the end of the year or at any time during the year under review.

REPORT OF THE DIRECTORS

SUBSTANTIAL SHAREHOLDERS

As at 31 October 2001, the register required to be kept under section 16(1) of the Securities (Disclosure of Interest) Ordinance (Chapter 396 of the Laws of Hong Kong) (“SDI Ordinance”) showed that the Company has been notified of the following interest, being 10% or more of the issued share capital of the Company. These interests are in addition to those disclosed above in respect of the Directors:–

Name	Number of Shares Held	Approximate percentage of Shareholding (%)
E-Teck Business Limited (<i>Note 1</i>)	42,828,254	12.24
Ever-Long Asset Management Limited (<i>Note 1</i>)	42,828,254	12.24
Ever-Long Holdings Limited (<i>Note 1</i>)	42,828,254	12.24
Styland Holdings Limited (<i>Notes 1 and 2</i>)	67,457,379	19.27

Notes:–

1. The 42,828,254 shares are beneficially owned by and registered in the name of E-Teck Business Limited. All the issued share capital of E-Teck Business Limited is beneficially owned by Ever-Long Asset Management Limited, which is a wholly-owned subsidiary of Ever-Long Holdings Limited. Ever-Long Holdings Limited is a wholly-owned subsidiary of Styland Holdings Limited which is a limited liability company incorporated in Bermuda whose shares are listed on the Main Board. Ever-Long Asset Management Limited, Ever-Long Holdings Limited and Styland Holdings Limited are all deemed to be interested in the shares held by E-Teck Business Limited for the purpose of the SDI Ordinance.
2. The 67,457,379 shares represents the 42,828,254 and 24,629,125 shares beneficially owned by and registered in the names of E-Teck Business Limited and Inworld System (HK) Limited respectively.

By virtue of Styland Holdings Limited’s over one-third indirect interest in Inworld System (HK) Limited as at 31 October 2001, Styland Holdings Limited was deemed to be interested in the shares held by Inworld System (HK) Limited.

MANAGEMENT SHAREHOLDERS

So far as the directors are aware, other than those disclosed under the section headed “Director’s Interest in Securities” above, there is no other person who is directly or indirectly interested in 5% or more of the share capital of the Company then issued and who is able, as a practical matter, to direct or influence the management of the Company.

PRE-EMPTIVE RIGHTS

There is no provision for pre-emptive rights under the Company’s Articles of Association or the laws of the Cayman Islands, which would oblige the Company to offer new shares on a pro rata basis to existing shareholders of the Company.

PURCHASE, SALE OR REPURCHASE OF SHARES

Since the shares of the Company commenced trading on GEM on 15 October 2001, neither the Company nor any of its subsidiaries had purchased, sold or repurchased any of the Company’s shares during the year.

REPORT OF THE DIRECTORS

SPONSOR'S INTEREST

As at 31 October 2001, neither DBS Asia Capital Limited ("DBS"), or its directors, employees or associates (as referred to in note 3 of Rule 6.35 of the GEM Listing Rules) had any interest in the securities of the Company or any member of Rainbow Group, or any right to subscribe for or to nominate persons to subscribe for the securities of the Company or any members of Rainbow Group.

Pursuant to the agreement dated 27 September 2001 entered into between the Company and the Sponsor, the Sponsor will receive a fee for acting as the Company's retained sponsor for the period from 15 October 2001 to 31 October 2003.

COMPETING INTEREST

None of the Directors or chief executive of the Company or its subsidiaries, the initial management shareholders or the substantial shareholders (as defined under the GEM Listing Rules) of the Company or their respective associates had any interest in a business which competes or may compete with the business of Rainbow Group.

CONNECTED TRANSACTIONS

Rainbow Group had related party transactions as further detailed in note 24 to the financial statements, which included the exempted continuing connection transaction described below and other related party transactions which were discontinued before the listing of the shares of the Company on GEM.

As disclosed in the sub-paragraph headed "Exempted continuing connected transaction" in the paragraphs headed "Connected transactions" under the section headed "Business of Rainbow Group" of the prospectus of the Company dated 28 September 2001, Ms. Li Ngar Kwan, Aldy, the chairperson of the Board and an executive Director and Newide International Limited, a subsidiary of the Company, entered into a lease agreement dated 1 June 2001. Pursuant to the lease agreement, Newide International Limited agreed to lease the factory premises located at Factory B on 4th Floor and Flat Roof of Sze Hing Loong Industrial Building, 44 Lee Chung Street, Chai Wan, Hong Kong from Ms. Li Ngar Kwan, Aldy for a term of three years commencing from 1 June 2001 at a monthly rent of HK\$21,000, exclusive of rates, management charges, air-conditioning fees and other outgoings. This transaction is exempted from reporting, announcement and independent shareholders' approval requirements under Rule 20.25(3) of the GEM Listing Rules as the annual total consideration of the transaction is less than HK\$1,000,000.

The independent non-executive Directors have reviewed the above transaction and confirmed that the transaction has been entered into in the ordinary and usual course of business of the Company, on normal commercial terms and in accordance with the said lease agreement on terms that are fair and reasonable and in the interests of the shareholders of the Company as a whole.

AUDIT COMMITTEE

The Company has established an audit committee with written terms of reference based on the guidelines recommended by the Hong Kong Society of Accountants. The audit committee comprises two independent non-executive Directors, namely Mr. Chiu Wai and Ms. Tam Fung Chee. Ms. Tam Fung Chee is also the chairperson of the audit committee of the board of Directors.

REPORT OF THE DIRECTORS

AUDIT COMMITTEE (continued)

The primary duties of the audit committee are to review the Company's annual report and accounts, half-year reports and quarterly reports and to provide advice and comments thereon to the board of Directors. The audit committee is also responsible for reviewing and supervising the Company's financial reporting and internal control procedures.

COMPLIANCE WITH RULES 5.28 TO 5.39 OF THE GEM LISTING RULES

The Company has complied with the board practices and procedures as set out in Rules 5.28 to 5.39 of the GEM Listing Rules since the listing of the Company's shares on GEM on 15 October 2001.

STAFF RETIREMENT SCHEME

Rainbow Group has implemented a provident fund scheme for its staff in compliance with the requirements of the Mandatory Provident Fund Schemes Ordinance ("MPF Ordinance") and strictly complies with the MPF Ordinance in making contributions and allows qualified employees to elect making voluntary contributions to the scheme.

AUDITORS

The financial statements of Rainbow Group were audited by Charles Chan, Ip & Fung CPA Ltd. A resolution for their reappointment as auditors for the ensuing year is to be proposed at the forthcoming annual general meeting of the Company.

On behalf of the Board

Ms. LI Ngar Kwan, Aldy
Chairperson

Hong Kong, 25 January 2002

AUDITORS' REPORT



Charles Chan, Ip & Fung CPA Ltd.
37th Floor, Hennessy Centre
500 Hennessy Road
Causeway Bay, Hong Kong

AUDITORS' REPORT TO THE SHAREHOLDERS OF RAINBOW INTERNATIONAL HOLDINGS LIMITED (INCORPORATED IN THE CAYMAN ISLANDS WITH LIMITED LIABILITY)

We have audited the financial statements on pages 34 to 64 which have been prepared in accordance with accounting principles generally accepted in Hong Kong.

RESPECTIVE RESPONSIBILITIES OF DIRECTORS AND AUDITORS

The Company's directors are responsible for the preparation of financial statements which give a true and fair view. In preparing financial statements which give a true and fair view it is fundamental that appropriate accounting policies are selected and applied consistently.

It is our responsibility to form an independent opinion, based on our audit, on those statements and to report our opinion to you.

BASIS OF OPINION

We conducted our audit in accordance with Statements of Auditing Standards issued by the Hong Kong Society of Accountants. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the Company's and the Group's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance as to whether the financial statements are free from material misstatement. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements. We believe that our audit provides a reasonable basis for our opinion.

OPINION

In our opinion the financial statements give a true and fair view of the state of affairs of the Company and of the Group as at 31 October 2001 and of the Group's loss and cash flows for the year then ended and have been properly prepared in accordance with the disclosure requirements of the Hong Kong Companies Ordinance.

Charles Chan, Ip & Fung CPA Ltd.
Certified Public Accountants
Hong Kong, 25 January 2002

Chan Wai Dune, Charles
Practising Certificate Number P00712

CONSOLIDATED INCOME STATEMENT

Year ended 31 October 2001

	Note	2001 HK\$'000	2000 HK\$'000
TURNOVER	3	110,047	126,157
COST OF SALES		<u>(72,269)</u>	<u>(79,972)</u>
GROSS PROFIT		37,778	46,185
OTHER REVENUE	3	1,080	7,085
OTHER EXPENSES			
Selling and distribution costs		(46,722)	(37,951)
Administrative expenses		(14,015)	(8,585)
		<u>(60,737)</u>	<u>(46,536)</u>
(LOSS)/PROFIT FROM OPERATIONS		(21,879)	6,734
FINANCE COSTS		<u>(3,924)</u>	<u>(4,174)</u>
(LOSS)/PROFIT BEFORE TAXATION	4	(25,803)	2,560
TAXATION	5	<u>–</u>	<u>(395)</u>
(LOSS)/PROFIT ATTRIBUTABLE TO SHAREHOLDERS	6	(25,803)	2,165
ACCUMULATED LOSSES BROUGHT FORWARD		<u>(2,138)</u>	<u>(4,303)</u>
ACCUMULATED LOSSES CARRIED FORWARD		<u>(27,941)</u>	<u>(2,138)</u>
(LOSS)/EARNINGS PER SHARE – BASIC	7a	(7.37) cents	0.62 cents
(LOSS)/EARNINGS PER SHARE – DILUTED	7b	<u>(7.02) cents</u>	<u>0.59 cents</u>

	<i>Note</i>	2001 <i>HK\$'000</i>	2000 <i>HK\$'000</i>
ASSETS			
Non-current assets			
Fixed assets	9	6,740	5,235
Investments in trust funds	11	8,530	–
		15,270	5,235
Current assets			
Due from a director	12	–	238
Due from related companies	13	–	31,889
Prepayments, deposits and other receivables		8,785	7,174
Inventories	14	27,597	23,238
Trade receivables		171	1,090
Cash and bank balance		29,104	147
		65,657	63,776
LIABILITIES			
Current liabilities			
Convertible loan notes	15	–	2,500
Due to a director	16	–	8,369
Bank overdrafts – secured		20,520	19,164
Current portion of interest-bearing borrowings – secured	17	4,393	9,459
Current portion of obligation under hire purchase contract	18	5	–
Trust receipt loans – secured		13,405	15,415
Trade payables		15,129	5,656
Other payables and accruals		13,687	6,002
Taxation payable	5	706	670
		67,845	67,235
Net current liabilities		(2,188)	(3,459)
Total assets less current liabilities		13,082	1,776
Non-current liabilities			
Interest-bearing borrowings – secured	17	469	3,840
Obligation under hire purchase contract	18	25	–
		494	3,840
		12,588	(2,064)
CAPITAL AND RESERVES			
Issued capital	20	3,500	74
Reserves	21	9,088	(2,138)
		12,588	(2,064)

Approved by the board of directors on 25 January 2002

On behalf of the board

LI Ngar Kwan, Aldy
Director

LIANG Kwong Lim
Director

The notes on pages 40 to 64 form an integral part of these financial statements.

BALANCE SHEET

As at 31 October 2001

	Note	2001 HK\$'000
ASSETS		
Non-current assets		
Investments in subsidiaries	10	4,193
Investments in trust funds	11	4,525
		8,718
Current assets		
Other receivables		407
Bank balance		16,124
		16,531
LIABILITIES		
Current liabilities		
Bank overdrafts – secured		340
Other payables		1,985
		2,325
Net current assets		14,206
Total assets less current liabilities		22,924
CAPITAL AND RESERVES		
Issued capital	20	3,500
Reserves	21	19,424
		22,924

Approved by the board of directors on 25 January 2002

On behalf of the board

LI Ngar Kwan, Aldy
Director

LIANG Kwong Lim
Director

CONSOLIDATED STATEMENT OF RECOGNISED GAINS AND LOSSES

Year ended 31 October 2001

	<i>Note</i>	2001 HK\$'000	2000 HK\$'000
(LOSS)/PROFIT FOR THE YEAR		(25,803)	2,165
GOODWILL ELIMINATED DIRECTLY AGAINST RESERVES	<i>21</i>	(10,707)	–
		<u>(36,510)</u>	<u>2,165</u>

The notes on pages 40 to 64 form an integral part of these financial statements.

CONSOLIDATED CASH FLOW STATEMENT

Year ended 31 October 2001

	<i>Note</i>	2001 <i>HK\$'000</i>	2000 <i>HK\$'000</i>
NET CASH INFLOW/(OUTFLOW) FROM OPERATING ACTIVITIES	22(a)	3,210	(11,738)
RETURNS ON INVESTMENTS AND SERVICING OF FINANCE			
Interest received		546	1,382
Interest paid		(3,924)	(4,174)
NET CASH OUTFLOW FROM RETURNS ON INVESTMENTS AND SERVICING OF FINANCE		(3,378)	(2,792)
TAXATION			
Hong Kong profits tax refund/(paid)		36	(76)
INVESTING ACTIVITIES			
Payment for purchase of fixed assets		(2,162)	(5,022)
Proceeds from sales of fixed assets		–	14,863
Investments in trust funds		(8,530)	–
Payment for purchase of subsidiaries	22(b)	(288)	–
NET CASH (OUTFLOW)/INFLOW FROM INVESTING ACTIVITIES		(10,980)	9,841
NET CASH OUTFLOW BEFORE FINANCING		(11,112)	(4,765)
FINANCING			
Proceeds from issue of ordinary shares		53,065	–
Share issue expenses		(6,945)	–
Proceeds from issue of convertible loan notes		1,000	2,500
New loans raised		9,887	9,300
Repayment of loans		(18,324)	(12,682)
Inception of hire purchase contract		31	–
Capital element of hire purchase contract paid		(1)	(89)
NET CASH INFLOW/(OUTFLOW) FROM FINANCING	22(c)	38,713	(971)
INCREASE/(DECREASE) IN CASH AND CASH EQUIVALENTS		27,601	(5,736)

CONSOLIDATED CASH FLOW STATEMENT (continued)

Year ended 31 October 2001

	<i>Note</i>	2001 <i>HK\$'000</i>	2000 <i>HK\$'000</i>
INCREASE/(DECREASE) IN CASH AND CASH EQUIVALENTS		27,601	(5,736)
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR		<u>(19,017)</u>	<u>(13,281)</u>
CASH AND CASH EQUIVALENTS AT END OF YEAR		<u>8,584</u>	<u>(19,017)</u>
ANALYSIS OF THE BALANCES OF CASH AND CASH EQUIVALENTS			
Cash and bank balance		29,104	147
Bank overdrafts		<u>(20,520)</u>	<u>(19,164)</u>
		<u>8,584</u>	<u>(19,017)</u>

The notes on pages 40 to 64 form an integral part of these financial statements.

NOTES TO THE FINANCIAL STATEMENTS

Year ended 31 October 2001

1. GROUP REORGANISATION AND BASIS OF PREPARATION

The Company was incorporated in the Cayman Islands on 6 March 2001 as an exempted company with limited liabilities under the Companies Law (Revised) of the Cayman Islands.

On 21 September 2001, pursuant to a group reorganisation scheme (“the Reorganisation”), the Company acquired the entire issued share capital of Rainbow Cosmetic (BVI) Limited (“Rainbow BVI”) through a share exchange as described in Note 20(d). Since then the Company became the holding company of the Rainbow BVI and its subsidiaries (collectively referred to as “Rainbow BVI Group”). The Company and Rainbow BVI Group are companies under common control and accordingly regarded as a continuing group. The Company and its subsidiaries are collectively referred to as (the “Group”). The Company’s shares were listed on the Growth Enterprise Market (the “GEM”) of The Stock Exchange of Hong Kong Limited on 15 October 2001.

Prior to the Reorganisation, on 11 November 2000, Newide International Limited (“Newide”), entered into a sale and purchase agreement to acquire all business and assets of a sole proprietorship namely Rainbow Trading Company (“RTC”) from Mr. Elbert Lee. Under the terms of the agreement, all business and assets of RTC were transferred to Newide after the close of business on 31 December 2000 at a consideration of HK\$1 paid by Newide. The results of the operations of RTC were included in the consolidated financial statements under the acquisition method of accounting from 1 January 2001, being the date immediately after the date of acquisition.

On 11 November 2000, Jet Legend Limited (“Jet Legend”), entered into two separate sale and purchase agreements to acquire all business and assets of a sole proprietorship namely Rainbow Cosmetic Company (“SRCC”) from Ms. Li Ngai Kwan, Aldy (“Ms. Aldy Li”), and of a partnership namely Rainbow Cosmetic Company (“PRCC”) from Ms. Aldy Li and her business partner.

Under the terms of the agreement, all business and assets of SRCC were transferred to Jet Legend after the close of business on 31 December 2000 at a consideration of HK\$3,500,000. The consideration was satisfied by issuance of shares in Jet Legend to Ms. Aldy Li. The results of the operations of SRCC were included in the consolidated financial statements under the merger accounting method.

Under the terms of the agreement, all business and assets of PRCC were transferred to Jet Legend after the close of business on 31 December 2000 at a consideration of HK\$500,000. The consideration was satisfied by issuance of shares in Jet Legend for an aggregate amount of HK\$200,000 to Ms. Aldy Li and HK\$300,000 paid to her business partner. The results of the operations of PRCC were included in the consolidated financial statements under the acquisition method of accounting from 1 January 2001, being the date immediately after the date of acquisition.

The consolidated financial statements include the results of operations of Rainbow Group as if the group structure resulting from the Reorganisation executed on 21 September 2001 had been in existence throughout the years ended 31 October 2000 and 2001 or since the dates of acquisition as described above or since the date of incorporation of the respective group companies where there was of a shorter period.

NOTES TO THE FINANCIAL STATEMENTS

Year ended 31 October 2001

1. GROUP REORGANISATION AND BASIS OF PREPARATION (continued)

During the year, the Group was engaged in investment holding, retailing and wholesaling of beauty products and provision of beauty services.

The Group's financial statements include the financial statements of the Company and its subsidiaries made up to 31 October. All significant intercompany transactions and balances within the Group are eliminated on consolidation.

2. PRINCIPAL ACCOUNTING POLICIES

The financial statements have been prepared in accordance with generally accepted accounting principles in Hong Kong and comply with Statements of Standard Accounting Practice issued by the Hong Kong Society of Accountants and the disclosure requirements of the Hong Kong Companies Ordinance and the Rules Governing the Listing of Securities on the GEM. The financial statements are prepared under the historical cost convention. Principal accounting policies are summarised below:

(a) Revenue recognition

- (i) Revenue from sale of goods is recognised on the transfer of risks and rewards of ownership, which generally coincides with the time when the goods are delivered to customers and title has passed.
- (ii) Revenue from provision of services is recognised when the services are rendered.
- (iii) Interest income is recognised on a time proportion basis, taking into account the principal amounts outstanding and the interest rates applicable.
- (iv) Operating lease rental income is recognised on a straight-line basis over the period of the respective leases.

(b) Borrowing costs

Borrowing costs are interests and other costs incurred in connection with the borrowings of funds. All borrowing costs are charged to the income statement in the year in which they are incurred.

(c) Goodwill and capital reserves

Goodwill, which represents the excess of purchase consideration over the fair values ascribed to the separable net assets of subsidiaries acquired at date of acquisition is written off directly to reserves in the year of acquisition. Negative goodwill is credited directly to reserves.

NOTES TO THE FINANCIAL STATEMENTS

Year ended 31 October 2001

2. PRINCIPAL ACCOUNTING POLICIES (continued)

(d) Fixed assets and depreciation

Fixed assets are stated at cost less accumulated depreciation and are depreciated at rates sufficient to write off their cost over their estimated useful lives on a straight-line basis. The principal annual rates are as follows:

Leasehold improvements	20% or over the lease term, if shorter
Equipment	20% to 33 $\frac{1}{3}$ %
Furniture and fixtures	20%

Major costs incurred in restoring fixed assets to their normal working condition are charged to the income statement. Improvements are capitalised and depreciated over their expected useful lives to the company.

The carrying amount of fixed assets are reviewed regularly to assess whether their recoverable amounts have declined below their carrying amounts. Expected future cash flows have not been discounted in determining the recoverable amount.

The gain or loss on disposal of fixed assets is the difference between the net sales proceeds and the carrying amount of the relevant asset, and is recognised in the income statement.

(e) Assets under leases

Leases that substantially transfer to the company all the rewards and risks of ownership of assets are accounted for as hire purchase contracts. At the inception of a hire purchase contract, the fair value of the asset is recorded together with the obligation, excluding the interest element, to pay future rentals.

Payments to the lessor are treated as consisting of capital and interest elements. Finance charges are debited to the income statement over the periods of the leases so as to produce an approximately constant periodic rate of charge on the remaining balances of the obligation for each accounting period.

Assets held under hire purchase contracts are depreciated over the shorter of the lease term and their estimated useful lives on the same basis as owned assets.

(f) Operating leases

Leases where substantially all the rewards and risks of ownership of assets remain with the leasing company are accounted for as operating leases. Rental payables under such operating leases are accounted for in the income statement on a straight-line basis over the periods of the respective lease.

NOTES TO THE FINANCIAL STATEMENTS

Year ended 31 October 2001

2. PRINCIPAL ACCOUNTING POLICIES (continued)

(g) Subsidiaries

A subsidiary is a company in which the company, directly or indirectly, controls more than half of its voting power or issued share capital or controls the composition of its board.

Investments in subsidiaries in the balance sheet are stated at cost less provision, if necessary, for any permanent diminution in value. The results of subsidiaries are accounted to the extent of dividends received and receivable.

(h) Investments in trust funds

Trust funds that the company intended to be held-to-maturity are stated at amortized cost, less provision for impairment losses.

Gain or loss on disposal of investments in trust funds, representing the difference between the net sale proceeds and the carrying amount of the trust funds, is recognised in the income statement in the period in which the disposal occurs.

(i) Related parties

Two parties are considered to be related if one party has the ability, directly or indirectly, to control the other party or exercise significant influence over the other party in making financial and operating decisions. Parties are also considered to be related if they are subject to common control or common significant influence.

(j) Inventories

Inventories are stated at the lower of cost and net realizable value. Cost, calculated on a first-in, first-out basis, comprises all costs of purchases, costs of conversion and other costs incurred in bringing the inventories to their present location and condition.

Net realizable value is the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sale.

(k) Trade receivables

Provision is made against trade receivables to the extent that they are considered to be doubtful. Trade receivables in the balance sheet is stated net of such provision.

(l) Cash equivalents

Cash equivalents are short-term, highly liquid investments which are readily convertible into known amounts of cash without notice and which were within three months of maturity when acquired; less advances from banks repayable within three months from the date of the advance. Cash equivalents include investments and advances denominated in foreign currencies provided that they fulfil the above criteria.

NOTES TO THE FINANCIAL STATEMENTS

Year ended 31 October 2001

2. PRINCIPAL ACCOUNTING POLICIES (continued)

(m) Deferred taxation

Deferred taxation is accounted for under the liability method in respect of timing differences between profit as computed for taxation purposes and profit as stated in the accounts to the extent that a liability or asset is expected with reasonable probability to crystallise in the foreseeable future. Deferred tax asset is not recognised unless its realization is assured beyond reasonable doubt.

(n) Translation of foreign currencies

Transactions in foreign currencies during the year are translated at exchange rates ruling at the transaction dates. Monetary assets and liabilities expressed in foreign currencies at the balance sheet date are translated at rates of exchange ruling at the balance sheet date. Exchange differences arising in these cases are dealt with in the income statement.

(o) Staff retirement benefits

The costs of staff retirement benefits are expensed in the period in which they are incurred.

3. TURNOVER AND REVENUE

Turnover represents the invoiced value of beauty products sold less discounts and sales returns and services income generated from the provision of beauty services.

	2001 <i>HK\$'000</i>	2000 <i>HK\$'000</i>
Turnover		
Retails and wholesales of beauty products	103,558	124,240
Beauty services	6,489	1,917
	110,047	126,157
Other revenue		
Rental income – Investment properties	–	192
Interest income	546	1,382
Exchange gain	123	21
Insurance compensation income	46	4,642
Surplus on fixed assets written off against insurance compensation	–	509
Sundry income	365	339
	1,080	7,085
Total revenue	111,127	133,242

NOTES TO THE FINANCIAL STATEMENTS

Year ended 31 October 2001

3. TURNOVER AND REVENUE (continued)

Turnover by principal activities and their respective contributions to (loss)/profit before taxation are:

	2001 (Loss) before taxation		2000 Profit before taxation	
	Turnover HK\$'000	HK\$'000	Turnover HK\$'000	HK\$'000
Retails and wholesales of beauty products	103,558	(25,689)*	124,240	2,162*
Beauty services	6,489	(114)	1,917	398
	<u>110,047</u>	<u>(25,803)</u>	<u>126,157</u>	<u>2,560</u>

No geographical analysis of Rainbow Group's turnover and their respective contribution to (loss)/profit before taxation is presented as all the turnover is attributable to business conducted in Hong Kong.

* The result of beauty services generated from turnover of approximately HK\$523,000 (2000: approximately HK\$1,244,000) has been included.

4. (LOSS)/PROFIT BEFORE TAXATION

(Loss)/profit before taxation is stated after crediting and charging the following:

	2001 HK\$'000	2000 HK\$'000
Crediting		
Rental income	–	192
Interest income	546	1,382
Net exchange gain	123	21
	<u>123</u>	<u>21</u>
Charging		
Auditors' remuneration		
Current year	360	336
Less: Over provision in previous years	(240)	–
	120	336
Cost of inventories sold (excluding provision for slow-moving inventory for the year)	71,819	79,501
Staff costs (excluding directors' remuneration)		
– Basic salaries and allowances	18,870	16,068
– Pension scheme contribution	795	–
Borrowing costs		
Interest on bank advances and other borrowings wholly repayable within 5 years	3,924	4,174
Depreciation		
Owned assets	3,621	2,139
Asset held under hire purchase contract	6	–
Operating lease rentals in respect of land and buildings	26,095	17,836
Provision for slow-moving inventories	450	471
Loss on disposal of fixed assets	–	303
	<u>–</u>	<u>303</u>

NOTES TO THE FINANCIAL STATEMENTS

Year ended 31 October 2001

5. TAXATION

Hong Kong profits tax has been provided for at the rate of 16% (2000: 16%) on the estimated assessable profits for the year.

The amount of taxation charged to the consolidated income statement represents:

	2001 <i>HK\$'000</i>	2000 <i>HK\$'000</i>
Hong Kong profits tax	–	498
Deferred taxation (<i>note 19</i>)	–	(103)
	<u>–</u>	<u>395</u>

Taxation in the consolidated balance sheet represents provision for taxation for prior years less amount of tax paid.

No provision for deferred taxation has been made for Rainbow Group for the year as the effect of all timing differences is not material.

Deferred taxation of Rainbow Group for the year has not been provided for in respect of the following:

	2001 <i>HK\$'000</i>	2000 <i>HK\$'000</i>
Accelerated depreciation allowances	200	400
Tax losses	(4,100)	(400)
	<u>(3,900)</u>	<u>–</u>

6. (LOSS)/PROFIT ATTRIBUTABLE TO SHAREHOLDERS

The (loss)/profit attributable to shareholders includes a profit of approximately HK\$15,000 (2000: HK\$Nil) which has been dealt with in the financial statements of the Company.

7. (LOSS)/EARNINGS PER SHARE

(a) Basic

The calculation of basic (loss)/earnings per share is based on the (loss) attributable to shareholders of approximately HK\$(25,803,000) (2000: a profit of approximately HK\$2,165,000) and the weighted average number of 350,000,000 (2000: 350,000,000) shares, after adjusting for the effects of capitalization issue deemed to be in issue throughout the year on the assumption that the Reorganisation had been completed on 1 November 1998 (pro forma formation date of the Group).

NOTES TO THE FINANCIAL STATEMENTS

Year ended 31 October 2001

7. (LOSS)/EARNINGS PER SHARE (continued)

(b) Diluted

The calculation of diluted (loss)/earnings per share is based on the (loss) attributable to shareholders of approximately HK\$(25,803,000) (2000: a profit of approximately HK\$2,165,000) and the 367,500,000 (2000: 367,500,000) shares, which represented the 350,000,000 shares deemed to be in issue throughout the year on the assumption that the Reorganisation had been completed on 1 November 1998 and after adjusting for the number of shares which are deemed to have been issued for no consideration under the Pre-IPO Share Option Scheme as defined in the prospectus of the Company dated 28 September 2001 based on the subscription price per share at HK\$0.25.

8. DIRECTORS' AND SENIOR MANAGEMENT'S EMOLUMENTS

(a) The emoluments of the Company's directors disclosed pursuant to Section 161 of the Companies Ordinance are as follows:

	2001 HK\$'000	2000 HK\$'000
Fees	–	–
Other emoluments		
Basic salaries, allowances and benefits in kind	1,497	241
Pension scheme contribution	25	–
	<u>1,522</u>	<u>241</u>

The number of directors whose emoluments fell within the following band:

	2001	2000
Executive directors		
Nil to HK\$1,000,000	3	4
HK\$1,000,001 to HK\$1,500,000	1	–
	<u>4</u>	<u>4</u>
Non-executive and independent non-executive directors		
Nil to HK\$1,000,000	3	3
	<u>3</u>	<u>3</u>

During the year ended 31 October 2001, the four executive directors received individual emoluments of approximately HK\$1,022,000 (2000: HK\$105,000), HK\$359,000 (2000: HK\$136,000), HK\$120,000 (2000: HK\$Nil) and HK\$20,000 (2000: HK\$Nil) respectively. Each of the non-executive and independent non-executive directors received director fees of HK\$Nil (2000: HK\$Nil).

No director waived any emoluments during the year. No payment as inducement to join or upon joining the Group or as compensation for loss of office was paid or is payable to any director.

NOTES TO THE FINANCIAL STATEMENTS

Year ended 31 October 2001

8. DIRECTORS' AND SENIOR MANAGEMENT'S EMOLUMENTS (continued)

In addition to the above emoluments, certain directors had share options granted under the Company's share option scheme. Details of these benefits in kind are disclosed under the paragraph "Directors' Interest in Securities" in the Directors' Report.

In the absence of a ready market for the share options granted on the shares of the Company, the directors are unable to arrive at an accurate assessment of the value of the share options granted to the respective directors.

Each of the executive directors has entered into a service contract with the Group during the year.

(b) Details of emoluments paid to the five highest paid individuals (including directors and other employees) were as follows:

	2001 <i>HK\$'000</i>	2000 <i>HK\$'000</i>
Basic salaries, allowances and benefits in kind	2,579	1,556
Pension scheme contribution	52	–
	<u>2,631</u>	<u>1,556</u>

Of the five highest paid individuals, two (2000: one) are directors whose emoluments are disclosed in note 8(a) above.

The number of five highest paid individuals (including directors and other employees) whose emoluments fell within the following band:

Directors	2001	2000
Nil to HK\$1,000,000	1	1
HK\$1,000,001 to HK\$1,500,000	1	–
	<u>2</u>	<u>1</u>
Other employees	2001	2000
Nil to HK\$1,000,000	3	4
	<u>3</u>	<u>4</u>

NOTES TO THE FINANCIAL STATEMENTS

Year ended 31 October 2001

9. FIXED ASSETS

The Group

	Leasehold improvements <i>HK\$'000</i>	Equipment <i>HK\$'000</i>	Furniture and fixtures <i>HK\$'000</i>	Motor vehicle <i>HK\$'000</i>	Total <i>HK\$'000</i>
Cost					
At 1/11/2000	6,222	1,303	3,258	540	11,323
Additions	<u>1,504</u>	<u>3,591</u>	<u>37</u>	<u>–</u>	<u>5,132</u>
At 31/10/2001	<u>7,726</u>	<u>4,894</u>	<u>3,295</u>	<u>540</u>	<u>16,455</u>
Accumulated depreciation					
At 1/11/2000	2,594	393	2,561	540	6,088
Charge for the year	<u>1,607</u>	<u>1,399</u>	<u>621</u>	<u>–</u>	<u>3,627</u>
At 31/10/2001	<u>4,201</u>	<u>1,792</u>	<u>3,182</u>	<u>540</u>	<u>9,715</u>
Net book value					
At 31/10/2001	<u>3,525</u>	<u>3,102</u>	<u>113</u>	<u>–</u>	<u>6,740</u>
At 31/10/2000	<u>3,628</u>	<u>910</u>	<u>697</u>	<u>–</u>	<u>5,235</u>

Note: The gross amount of asset held for use under hire purchase contract and the related accumulated depreciation charge at the balance sheet date of approximately HK\$31,000 (2000: HK\$Nil) and of approximately HK\$6,000 (2000: HK\$Nil) respectively.

10. INVESTMENTS IN SUBSIDIARIES

The Company

	2001
	<i>HK\$'000</i>
Investments at cost:	
Unlisted shares	1,097
Due from subsidiaries	6,146
Due to subsidiaries	<u>(3,050)</u>
	<u>4,193</u>

NOTES TO THE FINANCIAL STATEMENTS

Year ended 31 October 2001

10. INVESTMENTS IN SUBSIDIARIES (continued)

Notes:

(a) The amounts due from/(to) subsidiaries are unsecured and interest free.

(b) The following is a list of the subsidiaries at 31 October 2001:

Name of subsidiaries	Place of incorporation	Issued and fully paid share capital	Percentage of equity interest attributable to the Group		Principal activities
			Direct	Indirect	
Rainbow Cosmetic (BVI) Limited	British Virgin Islands	US\$50,000	100%		Investment holding
Rainbow Cosmetic Company Limited	Hong Kong	HK\$100		100%	Wholesaling and retailing of beauty products
Rainbow Cosmetic (Central) Company Limited	Hong Kong	HK\$100		100%	Retailing of beauty products
Newide International Limited	Hong Kong	HK\$10		100%	Wholesaling of beauty products
Nutriplus Cosmetics International Limited (Formerly known as Fans Cosmetics Limited)	Hong Kong	HK\$100		100%	Provision of beauty services
Jet Legend Limited	Hong Kong	HK\$2		100%	Wholesaling and retailing of beauty products
Rainbow HK Cosmetic Company Limited	Macau	MOP60,000		100%	Not yet commence business

Except for as disclosed in Note 15 to the financial statements, none of the subsidiaries had any loan capital in issue at any time during the year ended 31 October 2001.

NOTES TO THE FINANCIAL STATEMENTS

Year ended 31 October 2001

11. INVESTMENTS IN TRUST FUNDS

The Group

	2001 <i>HK\$'000</i>	2000 <i>HK\$'000</i>
Held-to-maturity debt securities, at cost Listed in Hong Kong	<u>8,530</u>	<u>–</u>
Market value	<u>8,239</u>	<u>–</u>

The Company

	2001 <i>HK\$'000</i>	2000 <i>HK\$'000</i>
Held-to-maturity debt securities, at cost Listed in Hong Kong	<u>4,525</u>	<u>–</u>
Market value	<u>4,524</u>	<u>–</u>

12. DUE FROM A DIRECTOR

The Group

	Mr. Elbert Lee <i>HK\$'000</i>
Balance at end of year	<u>–</u>
Balance at beginning of year	<u>238</u>
Maximum outstanding balance during the year	
– 2001	238
– 2000	<u>258</u>

The amount is unsecured, interest free and repayable on demand. At 31 October 2001 and 31 October 2000, there was no interest due and no provision for doubtful debt was made against the amount.

NOTES TO THE FINANCIAL STATEMENTS

Year ended 31 October 2001

13. DUE FROM RELATED COMPANIES

The Group

Name	Connected parties	Balance at end of year <i>HK\$'000</i>	Balance at beginning of year <i>HK\$'000</i>	Maximum outstanding balance during the year	
				2001 <i>HK\$'000</i>	2000 <i>HK\$'000</i>
Rainbow Trading Company (<i>Note b</i>)	Mr. Elbert Lee	–	26,917	26,917	26,917
Alpha Perfect Limited	Ms. Aldy Li	–	4,148	4,148	4,148
Rainbow Cosmetic Company (<i>Note c</i>)	Ms. Aldy Li	–	824	824	824
		<u>–</u>	<u>31,889</u>	<u>31,889</u>	<u>31,889</u>

Notes:

- The amounts are unsecured, interest free and repayable on demand. At 31 October 2001 and 31 October 2000 there was no interest due and no provision for doubtful debt was made against the amounts.
- On 11 November 2000, Newide entered into a sale and purchase agreement to acquire all business and assets (including all debts and liabilities) of RTC, a sole proprietorship owned by Mr. Elbert Lee. Therefore the amount has been transferred to Newide and eliminated on consolidation.
- On 11 November 2000, Jet Legend entered into a sale and purchase agreement to acquire all business and assets (including all debts and liabilities) of PRCC, a partnership owned by Ms. Aldy Li and her business partner. Therefore the amount has been transferred to Jet Legend and eliminated on consolidation.

14. INVENTORIES

The Group

	2001 <i>HK\$'000</i>	2000 <i>HK\$'000</i>
Merchandise	28,047	23,709
<i>Less: provision for slow-moving inventories</i>	450	471
	<u>27,597</u>	<u>23,238</u>

NOTES TO THE FINANCIAL STATEMENTS

Year ended 31 October 2001

15. CONVERTIBLE LOAN NOTES

The Group

On 19 October 2000, E-Teck Business Limited (“E-Teck”) entered into a subscription agreement (as supplemented by a supplemental deed dated 8 June 2001) with Rainbow BVI. Pursuant to the agreement, Rainbow BVI issued 5 convertible loan notes and 2 convertible loan notes of HK\$500,000 each i.e. HK\$2,500,000 and HK\$1,000,000 on 19 October 2000 and 4 December 2000 respectively.

The convertible loan notes carried interest at prime rate plus 2% per annum. Interest on the convertible loan notes is payable every six months in arrear commencing 19 April 2001.

On 14 September 2001, 8,750 shares of US\$1.00 each in the capital of Rainbow BVI were allotted and issued to E-Teck upon the exercise of the conversion right attaching to the convertible loan notes.

16. DUE TO A DIRECTOR

The Group

The amount due to a director is unsecured, interest free and repayable on demand.

17. INTEREST-BEARING BORROWINGS – SECURED

The Group

	2001 <i>HK\$'000</i>	2000 <i>HK\$'000</i>
Bank loans		
Repayable within one year	4,393	9,459
Repayable after one year but within two years	469	3,840
	4,862	13,299
Current portion of bank loans	<u>(4,393)</u>	<u>(9,459)</u>
	<u>469</u>	<u>3,840</u>

NOTES TO THE FINANCIAL STATEMENTS

Year ended 31 October 2001

18. OBLIGATION UNDER HIRE PURCHASE CONTRACT

The Group

Analysis of the capital element due under hire purchase contract is as follows:

	2001 <i>HK\$'000</i>	2000 <i>HK\$'000</i>
Repayable within one year	5	–
Repayable after one year but within two years	6	–
Repayable after two years but within five years	19	–
	30	–
Current portion of obligation under hire purchase contract	<u>(5)</u>	–
	<u>25</u>	<u>–</u>

19. DEFERRED TAXATION

The Group

	2001 <i>HK\$'000</i>	2000 <i>HK\$'000</i>
At 1 November	–	103
Transfer to taxation (<i>note 5</i>)	–	<u>(103)</u>
At 31 October	<u>–</u>	<u>–</u>
The potential deferred tax liability/(asset) not provided for in the financial statements amounts to:		
Accelerated depreciation allowances	400	200
Tax losses	<u>(4,500)</u>	<u>(400)</u>
	<u>(4,100)</u>	<u>(200)</u>

At the balance sheet date, there was no material unprovided deferred tax liabilities. Deferred tax assets arising from tax losses has not been recognised as it is uncertain that such an asset will be crystallised in the foreseeable future.

NOTES TO THE FINANCIAL STATEMENTS

Year ended 31 October 2001

20. ISSUED CAPITAL

	2001	
	Number of shares	HK\$'000
<i>Authorised:</i>		
Ordinary shares of HK\$0.01 each	<u>2,000,000,000</u>	<u>20,000</u>

		2001	
		Number of shares	HK\$'000
<i>Issued and fully paid</i>			
Issue of shares upon incorporation	(a) & (b)	10	–
Issue of shares arising from reorganisation	(d)	109,699,990	1,097
Private placement on 21 September 2001	(e)	6,300,000	63
Issue of shares through public offer and placing	(g)	60,000,000	600
Capitalisation issue	(h)	173,000,000	1,730
Remuneration shares	(f)	<u>1,000,000</u>	<u>10</u>
		<u>350,000,000</u>	<u>3,500</u>

Notes

- (a) The Company was incorporated in the Cayman Islands on 6 March 2001 with authorised share capital of HK\$350,000 divided into 3,500,000 shares of HK\$0.10 each, of which one share was issued and allotted for cash at par to the initial subscriber of the Company.
- (b) On 17 September 2001, the share capital of the Company was subdivided into 10 issued shares and 34,999,990 unissued shares.
- (c) On 21 September 2001, the authorised share capital of the Company was increased from HK\$350,000 to HK\$20,000,000 by the creation of 1,965,000,000 additional shares, such new shares to rank pari passu in all respects with the then existing shares.
- (d) On 21 September 2001, an aggregate of 109,699,990 shares were allotted and issued, credited as fully paid as consideration for the acquisition of the entire issued share capital of Rainbow BVI.
- (e) On 21 September 2001, 4,200,000 shares and 2,100,000 shares were issued and allotted to Ms. Aldy Li and Mr. Elbert Lee respectively at a subscription price of HK\$0.05 per share, which was fully paid in cash.
- (f) On 25 September 2001, the share premium of HK\$10,000 was capitalised and applied in paying up in full of 1,000,000 shares of HK\$0.01 each which were allotted and issued as fully paid to International Capital Network Limited (“ICN”), being part of the financial advisory fee (“Remuneration Shares”).
- (g) On 10 October 2001, 60,000,000 shares of HK\$0.01 each were issued at HK\$0.50 per share through public offer and placing (“New Issue”), resulting in net cash proceeds of approximately HK\$21,247,000.
- (h) Immediately after the New Issue, share premium of HK\$1,730,000 was capitalised and applied in paying up in full of 173,000,000 shares of HK\$0.01 each which were allotted and issued as fully paid on a pro-rata basis to the Company’s shareholders registered on 22 September 2001.

NOTES TO THE FINANCIAL STATEMENTS

Year ended 31 October 2001

21. RESERVES

The Group

	Share premium <i>HK\$'000</i>	Accumulated losses <i>HK\$'000</i>	Capital reserve* <i>HK\$'000</i>	Total <i>HK\$'000</i>
At 1/11/1999	–	(4,303)	–	(4,303)
Profit for the year	–	2,165	–	2,165
At 31/10/2000 as reported	–	(2,138)	–	(2,138)
Premium on issue of shares	29,892	–	–	29,892
Share issue expenses	(8,753)	–	–	(8,753)
Capitalisation of share premium	(1,730)	–	–	(1,730)
Loss for the year	–	(25,803)	–	(25,803)
Effect of the reorganisation	–	–	28,327	28,327
Goodwill written off	–	(10,707)	–	(10,707)
At 31/10/2001	<u>19,409</u>	<u>(38,648)</u>	<u>28,327</u>	<u>9,088</u>

* *Capital reserve of the Group represents the difference between the nominal value of the shares of subsidiaries acquired and the nominal value of shares issued by the Company as consideration thereof pursuant to the Reorganisation.*

The Company

	Share premium <i>HK\$'000</i>	Retained profits <i>HK\$'000</i>	Total <i>HK\$'000</i>
Premium on issue of shares	29,892	–	29,892
Share issue expenses	(8,753)	–	(8,753)
Capitalisation of share premium	(1,730)	–	(1,730)
Profit for the year	–	15	15
	<u>19,409</u>	<u>15</u>	<u>19,424</u>

Subject to the Cayman Islands Companies Law and Articles of Association, and provided that immediately following the distribution or payment of dividend, the Company is able to pay its debts as they fall due in the ordinary course of business, no dividend may be declared or paid other than out of profits and reserves of the Company lawfully available for distribution, including share premium.

NOTES TO THE FINANCIAL STATEMENTS

Year ended 31 October 2001

22. NOTES TO CASH FLOW STATEMENT

(a) Reconciliation of (loss)/profit before taxation to net cash inflow/(outflow) from operating activities

	2001 <i>HK\$'000</i>	2000 <i>HK\$'000</i>
(Loss)/profit before taxation	(25,803)	2,560
Depreciation	3,627	2,139
Loss on disposal of fixed assets	–	303
Interest income	(546)	(1,382)
Interest expenses	3,924	4,174
Decrease/(increase) in due from a director	13,551	(203)
Decrease/(increase) in due from related companies	3,192	(4,136)
Increase in prepayments, deposits and other receivables	(1,135)	(2,871)
Decrease/(increase) in inventories	4,318	(3,013)
Decrease/(increase) in trade receivables	920	(533)
Increase in trade payables	6,039	141
Increase in other payables and accruals	5,502	1,093
Decrease in due to a director	(8,369)	(11,234)
(Decrease)/increase in trust receipts loans – secured	(2,010)	1,224
	<hr/>	<hr/>
Net cash inflow/(outflow) from operating activities	<u>3,210</u>	<u>(11,738)</u>

NOTES TO THE FINANCIAL STATEMENTS

Year ended 31 October 2001

22. NOTES TO CASH FLOW STATEMENT (continued)

(b) Purchase of subsidiaries

	2001 <i>HK\$'000</i>	2000 <i>HK\$'000</i>
Net assets acquired:		
Fixed assets	70	–
Inventories	8,677	–
Prepayments and deposits	70	–
Due from related companies	85,110	–
Bank balance	12	–
Due to directors	13,313	–
Trade payables	(3,434)	–
Other payables and accruals	(218)	–
Due to related companies	(113,807)	–
Goodwill on consolidation	10,707	–
	<u>500</u>	<u>–</u>
Satisfied by:		
Cash consideration	300	–
Consideration shares	200	–
	<u>500</u>	<u>–</u>
Analysis of the net outflow of cash and cash equivalents in respect of the purchase of subsidiaries.		
	2001 <i>HK\$'000</i>	2000 <i>HK\$'000</i>
Cash consideration paid	300	–
Cash and cash equivalents acquired	(12)	–
Net outflow of cash and cash equivalents in respect of the purchase of subsidiaries	<u>288</u>	<u>–</u>

NOTES TO THE FINANCIAL STATEMENTS

Year ended 31 October 2001

22. NOTES TO CASH FLOW STATEMENT (continued)

(c) Analysis of changes in financing during the year

	Share Capital and share premium <i>HK\$'000</i>	Convertible loan notes <i>HK\$'000</i>	Bank loans <i>HK\$'000</i>	Obligation under hire purchase contract <i>HK\$'000</i>	Total <i>HK\$'000</i>
Balance as at 1 November 1999	–	–	16,681	89	16,770
Non cash movement					
New share issue for acquiring subsidiaries	74	–	–	–	74
	74	–	16,681	89	16,844
Issue of convertible loans note	–	2,500	–	–	2,500
New bank loans	–	–	9,300	–	9,300
Repayment of bank loans	–	–	(12,682)	–	(12,682)
Capital element of hire purchase contract paid	–	–	–	(89)	(89)
Balance as at 31 October 2000	74	2,500	13,299	–	15,873
Non cash movement					
Accruals for share issue expenses	(1,558)	–	–	–	(1,558)
New share issue for acquiring subsidiaries	1,097	–	–	–	1,097
Share swap for acquiring subsidiaries	(29,224)	–	–	–	(29,224)
Share issue for purchase of fixed assets	2,900	–	–	–	2,900
Conversion of convertible loan notes	3,500	(3,500)	–	–	–
	(23,211)	(1,000)	13,299	–	(10,912)
New shares issue of the Company	30,315	–	–	–	30,315
Share issue expenses	(6,945)	–	–	–	(6,945)
New shares issue of a subsidiary	22,750	–	–	–	22,750
Issue of convertible loan notes	–	1,000	–	–	1,000
New bank loans	–	–	9,887	–	9,887
Repayment of bank loans	–	–	(18,324)	–	(18,324)
Inception of hire purchase contract	–	–	–	31	31
Capital element of hire purchase contract paid	–	–	–	(1)	(1)
Net cash inflow/(outflow) from financing	46,120	1,000	(8,437)	30	38,713
Balance as at 31 October 2001	22,909	–	4,862	30	27,801

NOTES TO THE FINANCIAL STATEMENTS

Year ended 31 October 2001

22. NOTES TO CASH FLOW STATEMENT (continued)

(d) Major non-cash transactions

- (i) On 21 September 2001, an aggregate of 109,699,990 shares were allotted and issued, credited as fully paid as consideration for the acquisition of the entire issued share capital of Rainbow BVI.
- (ii) On 11 November 2000, Jet Legend entered into a sale and purchase agreement to acquire net assets of HK\$4,964,470. Consideration for this transaction was the issuance by Jet Legend of 4 shares of HK\$1 each credited as fully paid to Ms. Aldy Li. These shares were exchanged for capital of Rainbow BVI on 31 January 2001. The shares then were exchanged for capital of the Company on 21 September 2001.
- (iii) On 11 November 2000, Jet Legend entered into another sale and purchase agreement to acquire net assets of HK\$131,500. Consideration of this transaction was the issuance by Jet Legend of 4 shares of HK\$1 each credited as fully paid to Ms. Aldy Li and HK\$300,000 paid to her business partner. These shares were exchanged for capital of Rainbow BVI on 31 January 2001. The shares were then exchanged for capital of the Company on 21 September 2001.

23. SHARE OPTIONS

- (a) On 24 September 2001, pursuant to the Pre-IPO Share Option Scheme, options to subscribe for 35,000,000 shares were granted to certain directors, employees, consultants and advisers of the Group. The exercise price of the share options is HK\$0.25.

All of these options have a duration of three years from the commencement of the trading of the shares of the Company on the GEM.

Except for options granted to ICN as part of the remuneration for its financial advisory service rendered to the Group, each option shall lapse if the relevant grantee ceases to be a director or an employee of the Group or on any other ground set forth in the Pre-IPO Share Option Scheme.

During the year, no options were exercised under the Pre-IPO Share Option Scheme.

- (b) On 24 September 2001, the shareholders of the Company approved a share option scheme ("the Scheme") under which its Board of Directors may, at its discretion, offer full-time or part time employees and executive, non-executive and independent non-executive directors of the Company and/or any of its subsidiaries, options to subscribe for shares of the Company. The maximum number of shares in respect of which options may be granted under the Scheme shall not exceed 30% of the issued share capital of the Company. The subscription price will be determined by the Company's Board of Directors and will be less than the highest of (i) the nominal value of the shares, (ii) the quoted closing price of the Company's shares on the date of offer of the options, and (iii) the average of the quoted closing prices of the Company's shares on the five trading days immediately preceding the date of offer of the options.

During the year, no option was granted by the Company under the Scheme.

NOTES TO THE FINANCIAL STATEMENTS

Year ended 31 October 2001

24. RELATED PARTY TRANSACTIONS

Particulars of significant transactions between the Group and related parties during the year are summarised below:

	Note	2001 HK\$'000	2000 HK\$'000
Purchase of beauty products from a company connected with Ms. Aldy Li	(i)	2,091	–
Sales of beauty products to a company connected with Ms. Aldy Li	(i)	6	–
Purchase of beauty products from Rainbow Trading Company	(ii)	9,013	55,365
Sales of beauty products to Rainbow Cosmetic Company	(iii)	63	238
Purchase of beauty products from Rainbow Cosmetic Company	(iii)	–	52
Interest income received from Rainbow Trading Company	(ii)	367	1,382
Letter of credit handling fee income received from Rainbow Trading Company	(ii)	42	278
Rental expenses paid to Ms. Aldy Li	(iv)	<u>105</u>	<u>–</u>

Note:

- (i) The company connected with Ms. Aldy Li is owned by her brother.
- (ii) Mr. Elbert Lee was the sole proprietor of Rainbow Trading Company.
- (iii) Ms. Aldy Li was one of the two partners in the partnership, Rainbow Cosmetic Company.
- (iv) The Headquarter of the Group and the warehouse of Newide are located at the premises owned by Ms. Aldy Li. No rent was paid to Ms. Aldy Li for the year ended 31 October 2000 and until 1 June 2001. Ms. Aldy Li had entered into a lease agreement with Newide for the said premises for a term of 3 years commencing from 1 June 2001 at a monthly rent of HK\$21,000.
- (v) On 11 November 2000, Newide entered into a sale and purchase agreement to acquire all business and assets of a sole proprietorship namely RTC from Mr. Elbert Lee. Under the terms of the agreement, all business and assets of RTC with the net liabilities in the sum of approximately HK\$10,338,000 were transferred to Newide after the close of business on 31 December 2000 at a nominal consideration of HK\$1 paid by Newide, the consideration of which was determined on arm's length basis and after negotiations with the relevant parties.

NOTES TO THE FINANCIAL STATEMENTS

Year ended 31 October 2001

24. RELATED PARTY TRANSACTIONS (continued)

- (vi) On 11 November 2000, Jet Legend entered into two separate sale and purchase agreements to acquire all business and assets of a sole proprietorship namely SRCC from Ms. Aldy Li and a partnership namely PRCC from Ms. Aldy Li and her business partner.

Under the terms of the agreement, all business and assets of SRCC with the net assets in the sum of approximately HK\$4,964,000 were transferred to Jet Legend after the close of business on 31 December 2000 at a consideration of HK\$3,500,000, which was determined on arm's length basis and after negotiations with the relevant parties. The consideration was satisfied by issuance of shares in Jet Legend to Ms. Aldy Li.

Under the terms of the agreement, all business and assets of PRCC with the net assets in the sum of approximately HK\$132,000 were transferred to Jet Legend after the close of business on 31 December 2000 at a consideration of HK\$500,000 which was determined on arm's length basis and after negotiations with the relevant parties. The consideration was satisfied by issuance of shares in Jet Legend for an aggregate amount of HK\$200,000 to Ms. Aldy Li and HK\$300,000 paid to her business partner.

The directors of the Company are of the opinion that the above transactions were conducted under normal commercial terms in the usual course of business.

25. COMMITMENTS

At 31 October 2001, the total future minimum lease payments under non-cancellable operating leases are payable as follows:

	2001 <i>HK\$'000</i>	2000 <i>HK\$'000</i>
Within one year	21,364	17,103
In the second to fifth years inclusive	13,591	10,255
	<u>34,955</u>	<u>27,358</u>

NOTES TO THE FINANCIAL STATEMENTS

Year ended 31 October 2001

26. BANKING FACILITIES AND PLEDGE OF ASSETS

At 31 October 2001, the Group's total available banking facilities of approximately HK\$38,384,000 of which of approximately HK\$33,566,000 was utilised. These facilities were secured by the following:–

- (i) Bank fixed deposits of approximately HK\$12 million and units of trust fund of the Group.
- (ii) Corporate guarantee executed by Jet Legend of approximately HK\$10 million.
- (iii) Corporate guarantee executed by the Company of approximately HK\$9 million.
- (iv) Legal charges on certain properties and units of trust fund held by, and the fixed deposits maintained in the name of Ms. Aldy Li.
- (v) Personal guarantee executed by Ms. Aldy Li.
- (vi) Fixed deposits held by an individual connected with Ms. Aldy Li.

Subsequent to the balance sheet date, on 14 January 2002, the personal guarantee executed by Ms. Aldy Li, units of trust fund held by, and the fixed deposits maintained in the name of Ms. Aldy Li as security for the banking facilities granted by Shanghai Commercial Bank Limited has been released.

The release of the legal charges on fixed deposits held by an individual connected with Ms. Aldy Li as security for the banking facilities granted by Shanghai Commercial Bank Limited is still under negotiation. The Directors are of the opinion that the release of security could be completed shortly.

The release of the personal guarantee executed by Ms. Aldy Li and fixed deposits maintained in the name of Ms. Aldy Li as security for the banking facilities granted by Hang Seng Bank Limited is still under negotiation. The Directors are of the opinion that the release of security could be completed shortly.

The release of the legal charges on certain properties held by, and fixed deposits maintained in the name of Ms. Aldy Li as security for the banking facilities granted by Chekiang First Bank Limited is still under negotiation. The Directors are of the opinion that the release of security could be completed shortly.

27. STAFF RETIREMENT SCHEME

The Group has implemented a provident fund scheme for its staff in compliance with the requirements of the Mandatory Provident Fund Schemes Ordinance effective from 1 December 2000. The retirement scheme contributions charged to the income statement represent contributions payable (i.e. 5% of staff's relevant income with upper monthly limit of HK\$1,000) by the Group to the specified retirement fund of the individual employees. During the year ended 31 October 2001, the aggregate amount of employer's contribution made by the Group to the retirement scheme was approximately HK\$820,000 (2000: HK\$Nil).

NOTES TO THE FINANCIAL STATEMENTS

Year ended 31 October 2001

28. CHANGE OF NAME

The Company changed its corporate name from “Rainbow Cosmetic International Holdings Limited also known as 彩虹化粧品國際控股有限公司” to “Rainbow International Holdings Limited also known as 彩虹國際控股有限公司” on 11 September 2001.

29. CONTINGENT LIABILITIES

As at 31 October 2001, the Company had guarantees given to banks for banking facilities utilised by certain subsidiaries to the extent of approximately HK\$9 million.

Apart from the above, the Group and the Company had no material litigation or contingent liabilities as at 31 October 2001 and up to the date of the approval of the financial statements.

NOTICE OF ANNUAL GENERAL MEETING

NOTICE IS HEREBY GIVEN THAT the annual general meeting (“Annual General Meeting”) of the shareholders of Rainbow International Holdings Limited (the “Company”) will be held at 1st Floor, 8 Kai Chiu Road, Causeway Bay, Hong Kong on 28 February 2002 at 9:00 a.m. for the following purposes:

1. To receive and consider the audited financial statements of the Company and the reports of the directors (“Directors”) and auditors of the Company for the year ended 31 October 2001.
2. To re-elect Directors and to authorize the board of Directors (“Board”) to fix the remuneration of the Directors.
3. To re-appoint auditors of the Company and to authorize the Board to fix their remuneration.
4. As special business, to consider and if thought fit, to pass the following resolution as an ordinary resolution:

“THAT:

- (a) subject to paragraph (c) of this resolution, and pursuant to the Rules Governing the Listing of Securities on the Growth Enterprise Market (“GEM”) of The Stock Exchange of Hong Kong Limited (“Stock Exchange”), the exercise by the Directors during the Relevant Period (as hereinafter defined) of all the powers of the Company to allot, issue and deal with additional shares in the capital of the Company (“Shares”) and to make or grant offers, agreements and options which might require the exercise of such powers be and is hereby generally and unconditionally approved;
- (b) the approval in paragraph (a) of this resolution shall be in addition to any other authorisation given to the Directors and shall authorize the Directors during the Relevant Period to make or grant offers, agreements and options which might require the exercise of such powers after the end of the Relevant Period;
- (c) the aggregate nominal amount of share capital allotted or agreed conditionally or unconditionally to be allotted (whether pursuant to options or otherwise) by the Directors pursuant to the approval in paragraph (a) of this resolution, otherwise than pursuant to (i) a Rights Issue (as defined below); or (ii) the grant or exercise of any options under the share option scheme of the Company or any other option scheme or similar arrangement for the time being adopted for the grant or issue of Shares or rights to acquire Shares; or (iii) any scrip dividend or similar arrangement providing for the allotment of Shares in lieu of the whole or part of a dividend on Shares in accordance with the memorandum of association and articles of association of the Company in force from time to time, shall not exceed 20 per cent of the aggregate nominal amount of the share capital of the Company in issue as at the date of the passing of this resolution and the approval in paragraph (a) of this resolution shall be limited accordingly; and

NOTICE OF ANNUAL GENERAL MEETING

(d) for the purpose of this resolution:

“Relevant Period” means the period from the date of the passing of this resolution until whichever is the earliest of:

- (i) the conclusion of the next annual general meeting of the Company;
- (ii) the expiration of the period within which the next annual general meeting of the Company is required by the articles of association of the Company or any applicable laws of the Cayman Islands to be held; and
- (iii) the date on which the authority given under this resolution is revoked or varied by an ordinary resolution of the shareholders of the Company in general meeting.

“Rights Issue” means an offer of Shares, or offer or issue of warrants, options or other securities giving rights to subscribe for Shares open for a period fixed by the Company or the Directors to holders of Shares on the register of members of the Company on a fixed record date in proportion to their then holdings of Shares (subject to such exclusions or other arrangements as the Directors may deem necessary or expedient in relation to fractional entitlements or having regard to any restrictions or obligations under the laws of, or the requirements of, any jurisdiction or any recognized regulatory body or any stock exchange applicable to the Company).”

5. As special business, to consider and, if thought fit, to pass the following resolution as an ordinary resolution:

“THAT:

- (a) subject to paragraph (b) of this resolution, the exercise by the Directors during the Relevant Period (as hereinafter defined) of all powers of the Company to purchase its shares on the GEM or any other stock exchange on which the Shares may be listed and which is recognized by The Securities and Futures Commission of Hong Kong (“Securities and Futures Commission”) and the Stock Exchange for such purpose, in accordance with the rules and regulations of the Securities and Futures Commission, the Stock Exchange or of any such other stock exchange from time to time and all applicable laws in this regard, be and is hereby generally and unconditionally approved;
- (b) the aggregate nominal amount of Shares which may be purchased by the Company pursuant to the approval in paragraph (a) of this resolution during the Relevant Period shall not exceed 10 per cent of the aggregate nominal amount of the issued share capital of the Company as at the date of the passing of this resolution and the authority pursuant to paragraph (a) of this resolution shall be limited accordingly; and

NOTICE OF ANNUAL GENERAL MEETING

- (c) for the purpose of this resolution, “Relevant Period” means the period from the date of the passing of this resolution until whichever is the earliest of:
 - (i) the conclusion of the next annual general meeting of the Company;
 - (ii) the expiration of the period within which the next annual general meeting of the Company is required by the articles of association of the Company, or any applicable laws of the Cayman Islands to be held; and
 - (iii) the date on which the authority given under this resolution is revoked or varied by an ordinary resolution of the shareholders of the Company in general meeting.”

6. As special business, to consider and, if thought fit, to pass the following resolution as an ordinary resolution:

“**THAT** conditional upon resolutions nos. 4 and 5 above being duly passed, the unconditional general mandate granted to the Directors to exercise the powers of the Company to allot, issue and deal with additional Shares pursuant to resolution no. 4 above be and is hereby extended by the addition to the aggregate nominal amount of the share capital which may be allotted or agreed conditionally or unconditionally to be allotted and issued by the Directors of the Company pursuant to such general mandate of an amount representing the aggregate nominal amount of the share capital of the Company repurchased by the Company under the authority granted pursuant to resolution no. 5 above, provided that such amount shall not exceed 10 per cent of the aggregate nominal amount of the issued share capital of the Company as at the date of the passing of this resolution.”

By Order of the Board
Rainbow International Holdings Limited
Lo Yu Wah
Company Secretary

Hong Kong, 31 January 2002

Principal place of business:
Flat B, 4th Floor
Sze Hing Loong Industrial Building
44 Lee Chung Street
Chaiwan
Hong Kong

NOTICE OF ANNUAL GENERAL MEETING

Notes:

1. A shareholder of the Company entitled to attend and vote at the meeting is entitled to appoint a person or persons (if he holds two or more Shares) as his proxy or proxies to attend and vote instead of him. A proxy need not be a shareholder of the Company.
2. To be valid, a form of proxy, together with the power of attorney or other authority (if any) under which it is signed or a notarially certified copy of that power of attorney or authority, must be deposited with the branch share registrar of the Company in Hong Kong, Standard Registrars Limited, 5th Floor, Wing On Centre, 111 Connaught Road Central, Hong Kong, not less than 48 hours before the time appointed for holding the meeting or any adjourned meeting, and in default thereof the form of proxy shall not be treated as valid. No instrument appointing a proxy shall be valid after the expiry of 12 months from the date of its execution.
3. An explanatory statement containing further details regarding resolution numbered 5 above as required by the Rules Governing the Listing of Securities on the Growth Enterprise Market of the Stock Exchange will be dispatched to the members of the Company together with the 2001 Annual Report.
4. Delivery of an instrument appointing a proxy shall not preclude a shareholder from attending and voting in person at the meeting if the shareholder so desires and in such event the instrument appointing a proxy shall be deemed to be revoked.