

# **QINGMEI GROUP HOLDINGS LIMITED**

**清美集團控股有限公司**

(Incorporated in the Cayman Islands with registration number CT-230192)

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## **RESPONSE TO QUERIES FROM THE SINGAPORE EXCHANGE SECURITIES TRADING LIMITED (“SGX-ST”) ON THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 30 JUNE 2014 (“RESULTS ANNOUNCEMENT”)**

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In response to the queries raised by the SGX-ST in its email dated 18 September 2014, the Board of Directors of QingMei Group Holdings Limited (the “Company”) would like to provide the following explanation in relation to the Results Announcement dated at 29 August 2014:-

### **Query 1:**

**The Company provided an impairment loss on property, plant and equipment of RMB56 million and land use rights of RMB50.8 million. To disclose:**

- a. Reason for decline in value of land use rights of 64% from RMB82.5 million to RMB29.9 million. To provide details of the land use rights and the significant impairment in value of land use rights. Please also disclose the valuation methodologies and major assumptions.**
- b. Breakdown of the major classes by property, plant and equipment impaired and reasons for impairment when revenue increased by 56.9% on the back of an increase in sales quantity of 81.4%. To provide basis and major assumptions for significant decrease in valuation even though the Company reported improved assets utilization of production facilities.**

### **Company’s Response:**

In response to the questions on the impairment loss on land use rights and property, plant and equipment, please note the following rationale when the Company was performing impairment testing for non-financial assets as at the year end:

#### **(a)**

For the purposes of impairment testing, land use rights and property, plant and equipment have been allocated to a Cash Generating Unit (“CGU”) of the Group, relating to the manufacturing and trading of shoe soles in the PRC (the “Shoe Soles Business”).

In view of the sustained operating losses of the Shoe Soles Business and the price pressure faced from the intense competition in the industry of manufacturing and trading of shoe soles during the year, there is an indication of impairment for the CGU of the Shoe Soles Business operated. The management reviewed the carrying amounts of the Group's land use rights, and property, plant and equipment, with reference to the valuation of the value-in-use of the CGU and the corresponding individual fair market valuation of the above-mentioned assets performed by independent qualified professional surveyors. The management adopted the fair market valuation of the assets as the recoverable amount of the assets in the impairment review.

Land use rights of the Group refer to the 9 State-owned Land Use Rights Certificates dated 2 September 2009 with a total site area of 46,174 sq.m., which have been granted to Qingmei (China) Company Limited for a term expiring on 24 August 2059 for industrial purpose.

Land use rights have been allocated to the CGU of the Shoe Soles Business and the impairment assessment of this CGU as mentioned above. Impairment loss on land use rights amounted to approximately RMB50.8 million and was charged under other expenses in profit or loss during the year with reference to the valuation of the fair market value of the land use rights performed by independent qualified professional surveyors.

The valuation of the land use rights and property, plant and equipment of the Group is determined by applying the market approach, taking into account the sales prices recently for similar assets to those comprising the CGU and related market data with adjustments made to the indicated market prices to reflect the conditions and utilities of the appraised assets relative to their market comparable.

The valuation has been made on the assumption that the asset is sold in the market without the benefit of deferred terms contract, leaseback, joint venture, management agreement or any other similar arrangement which would serve to affect the value of the property. In addition, no account has been taken of any option or right of pre-emption concerning or effecting the sale of the asset and no forced sale situation in any manner is assumed in the valuation.

**(b)**

The breakdown of the major classes of property, plant and equipment impaired is as follows:

	<b>Leasehold Buildings RMB'000</b>	<b>Plant and machinery RMB'000</b>	<b>Furniture, fixtures and office equipment RMB'000</b>	<b>Total RMB'000</b>
Impairment loss for the year	(38,195)	(17,655)	(177)	(56,027)

Even though the revenue and sales quantity of the Company increased by 56.9% and 81.4% respectively as compared to that of FY2013, the production scale of the Company has not reached the optimal operation level to breakeven. As a result, the Company resulted in a gross loss of RMB78.4 million in FY2014 as compared to a gross loss of RMB61.8 million in FY2013. Even though there is an improvement in the gross loss ratio from 37.5% in FY2013 to 30.4% in FY2014 due to the improved assets utilization of production facilities resulted from increased sales in FY2014, the management expects the Group's existing core businesses to remain challenging as further softening of customers' demand for the entire sport shoes industry continues to make recovery to profitability difficult and increase pressure in pricing our products in the market. An impairment review of the carrying value of the Group's assets has been conducted, with reference to the valuations performed by the independent qualified professional surveyors as mentioned in query 1(a). Impairment losses were made on land use rights, and property, plant and equipment totally of approximately RMB106.9 million, of which impairment losses on property, plant and equipment was amounted to approximately RMB56.0 million with reference to the valuation of the fair market value of the property, plant and equipment performed by the independent qualified professional surveyors. The impairment losses were charged under other expenses in profit and loss during the year.

The valuation has been made on the same assumption that mentioned in our reply to query 1(a) above.

## **Query 2:**

We note the Company's disclosure on page 10 that the rental income increased by RMB1 million during FY2014. To provide details of the investment properties and elaborate on the reasons for the RMB14.7 million decrease in fair value in investment properties. Please also elaborate on the "fair value" approach undertaken for the valuation of investment properties.

## **Company's Response:**

The details of the investment properties are as follows:

<b>Location</b>	<b>Description and existing use</b>	<b>Approximate site area (sq.m.)</b>	<b>Term of lease</b>
Sucuo Village Chendai Town Jinjiang City, Fujian Province The People's Republic of China	An office and research complex	The properties have a total gross floor area of approximately 18,115 sq.m.	The property is subject to a land use right till 24 August 2059 for industrial purpose

The rental income of the Company started from May 2013 upon transfer of owner-occupied leasehold buildings and land use rights to investment properties. As a result, the increase of RMB1 million actually resulted from the increase in the number of months that contributed rental income (FY2014:12 months, FY2013: 2 months). The decrease in fair value in investment properties was mainly due to a lower rental per sq.m. in the lease agreements signed during the year which decreased from approximately RMB12 per sq.m. in FY2013 to approximately RMB9 per sq.m. in FY2014 resulting from the decrease in the demand of industrial land and properties and the Company's effort to reduce vacancy of the investment properties during the year.

The fair values of the investment properties at 30 June 2014 are determined by independent qualified professional surveyors who have recent experience in the location and category of the investment properties being valued. The valuation was based on the income approach where appropriate by taking into account the current rents of the property being held under existing tenancies and the reversionary potential of the tenancies if they have been or would be let to tenants.

**Query 3:**

We note that trade receivables increased by 214.7% to RMB128.7 million. On the other hand, sales increased by 56.9% to RMB258.3 million. On the trade receivables, to provide:

- a. **Details of the extension settlement period offered.**

**Company's Response:**

In response to the recent poor business environment in the sports footwear retail market in the PRC, the Company has offered to the customers an extension of the settlement period in which trade receivables generally have credit terms ranging from 90 days to 180 days (2013: 60 days to 90 days) in order to stimulate the sales of the Company during the year.

- b. **Aging analysis.**

**Company's Response:**

Ageing analysis of trade receivables that are neither individually nor collectively considered to be impaired is as follows:

	<b>2014</b>
	<b>RMB'000</b>
Neither past due nor impaired	<b>125,579</b>
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1 - 30 days past due	<b>1,967</b>
31 - 60 days past due	<b>295</b>
61 - 180 days past due	<b>851</b>
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	<b>3,113</b>
Total trade receivables net of provision for impairment	<b>128,692</b>
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- c. Reasons why customers were unable to repay within the settlement period and efforts taken by the Company to collect its debts.**

**Company's Response:**

In recent years, the sports footwear retail market in China has been struggling with slowing demand, excessive inventory build-up, lack of innovation and over-expansion. The retail sector has also faced increasing macro-economic challenges and intense price competitive. As a result, certain customers experienced challenges from the poor industrial environment mentioned and tightened credit control of bank borrowings in the PRC. For certain slow moving trade debtors, the Group ceased to supply goods to them and letters of demand had been issued to chase for the repayment of outstanding balances. In the meantime, the Group is still working to collect the outstanding debts from the impaired trade receivables and relevant sales personnel are tasked to liaise and meet up with them regularly to follow up with the repayment.

- d. Any major customers. If yes, to provide details.**

**Company's Response:**

The trade receivables portfolio is diversified into over 60 customers, of which one customer's individual gross trade receivables balance contributed over 10% of the total gross trade receivables as at the year ended which amounted to a total of approximately RMB15.7 million.

**Query 4:**

**It was disclosed on page 14 that there was a prepayment of the new research projects for development of new raw materials for production of RMB4.6 million. To provide details on this new research project and the reasons for the Company having to prepay for such projects.**

**Company's Response:**

The new research projects are related to mid-high end, new generation shoe soles which enable the Group to improve in the quality, appearance, durability and functionality of sport shoe soles. Advance payment to research institutions was required to carry out further research into new and improved materials for our midsoles to improve the shock absorption and breathability properties.

**Query 5:**

**It was disclosed on page 14 that there was a “full settlement of certain outstanding balance amounted to RMB7.8 million owing to the fixed assets vendors following completion of construction works for its multi-complex buildings in FY2013”. To provide details of the current usage of this multi-complex building by the Company and whether this has been fully tenanted.**

**Company's Response:**

The multi-complex building represents the investment property of the Group with a total gross floor area of approximately 18,115 sq.m. which has been fully tenanted as at the year ended.

Submitted by Mr. Su Shu Biao, Executive Chairman and Chief Executive Officer, on 22 September 2014 to the SGX-ST