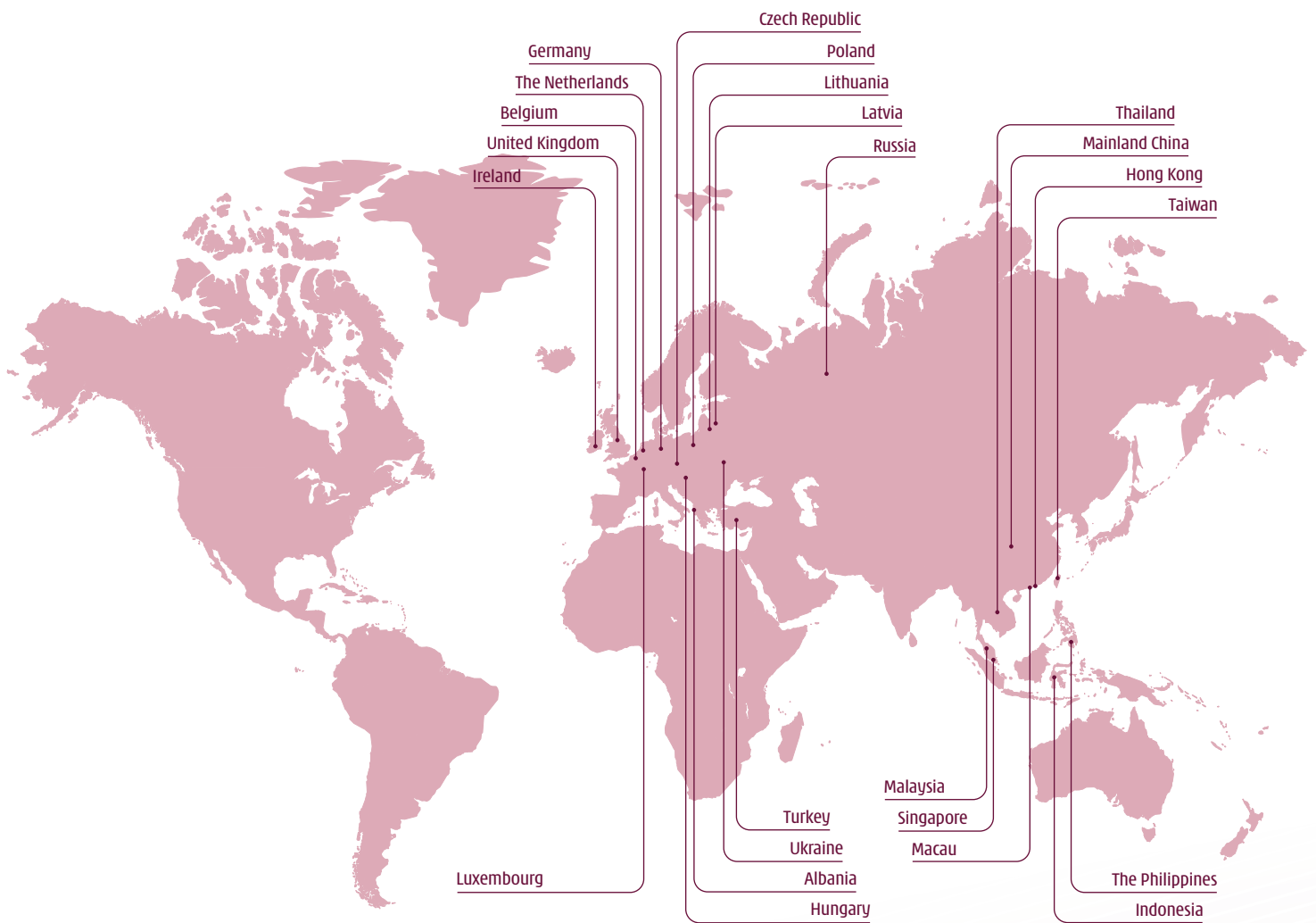


Operations Review



Watsons rolls out the fun and youth-oriented G Next store in Shanghai to bring a new shopping experience to young customers.

Retail





1. The Perfume Shop is the largest fragrance-only retailer in the UK and Ireland.
2. The number of Superdrug's stores exceeds 800 in the UK and Ireland.
3. ICI PARIS XL opens a stylish and luxurious new concept store to give beauty-lovers a refreshing experience.



4. Watsons Malaysia offers a wide range of health and beauty products.

5. Savers offers competitively priced health and beauty products in over 400 stores on the High Street in the UK.

Operations Review – Retail

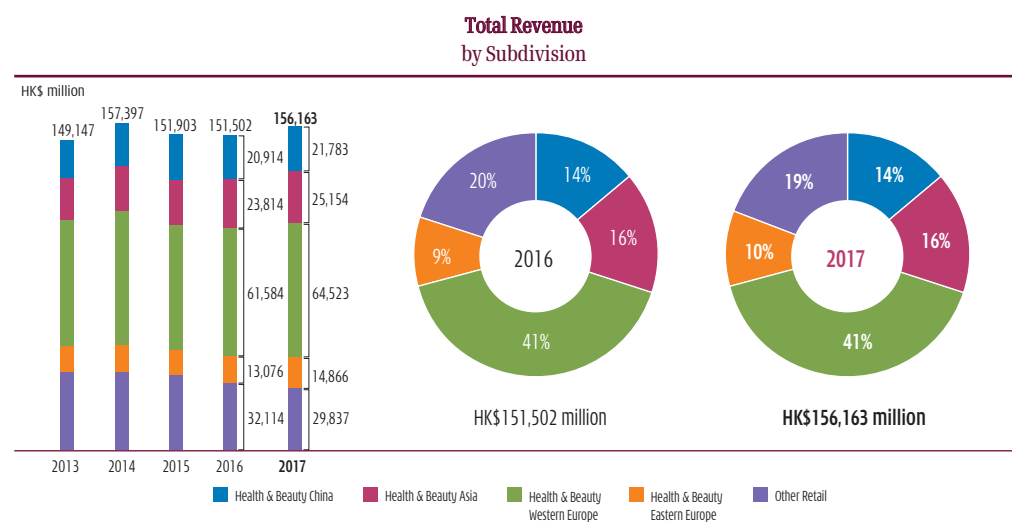
The retail division consists of the A S Watson (“ASW”) group of companies, the largest health and beauty retailer in Asia and Europe in terms of store numbers.

Group Performance

ASW operated 13 retail brands with over 14,000 stores in 24 markets worldwide in 2017, providing high quality personal care, health and beauty products; food and fine wines; as well as consumer electronics and electrical appliances. ASW also manufactures and distributes bottled water and other beverages in Hong Kong and the Mainland.

	2017 HK\$ million	2016 HK\$ million	Change	Change in Local Currency
Total Revenue	156,163	151,502	+3%	+2%
EBITDA	14,798	14,567	+2%	–
EBIT	12,089	12,059	–	-2%
Total Store Numbers	14,124	13,331	+6%	

Total reported revenue was 3% ahead of last year, driven by a 6% increase in store numbers, primarily in Health and Beauty China and Asia, as well as an overall 0.9% comparable stores sales growth.



Total Revenue	2017 HK\$ million	2016 HK\$ million	Change	Change in Local Currency
Health & Beauty China	21,783	20,914	+4%	+5%
Health & Beauty Asia	25,154	23,814	+6%	+6%
Health & Beauty China & Asia Subtotal	46,937	44,728	+5%	+6%
Health & Beauty Western Europe	64,523	61,584	+5%	+3%
Health & Beauty Eastern Europe	14,866	13,076	+14%	+7%
Health & Beauty Europe Subtotal	79,389	74,660	+6%	+4%
Health & Beauty Subtotal	126,326	119,388	+6%	+5%
Other Retail ⁽¹⁾	29,837	32,114	-7%	-7%
Total Retail	156,163	151,502	+3%	+2%

Comparable Stores Sales Growth (%) ⁽²⁾	2017	2016
Health & Beauty China	-4.3% ⁽³⁾	-10.1% ⁽³⁾
Health & Beauty Asia	+3.8%	+1.9%
Health & Beauty China & Asia Subtotal	—	-4.0%
Health & Beauty Western Europe	+2.1%	+3.7%
Health & Beauty Eastern Europe	+4.4%	+4.6%
Health & Beauty Europe Subtotal	+2.5%	+3.8%
Health & Beauty Subtotal	+1.6%	+1.0%
Other Retail ⁽¹⁾	-2.3%	-8.2%
Total Retail	+0.9%	-0.8%

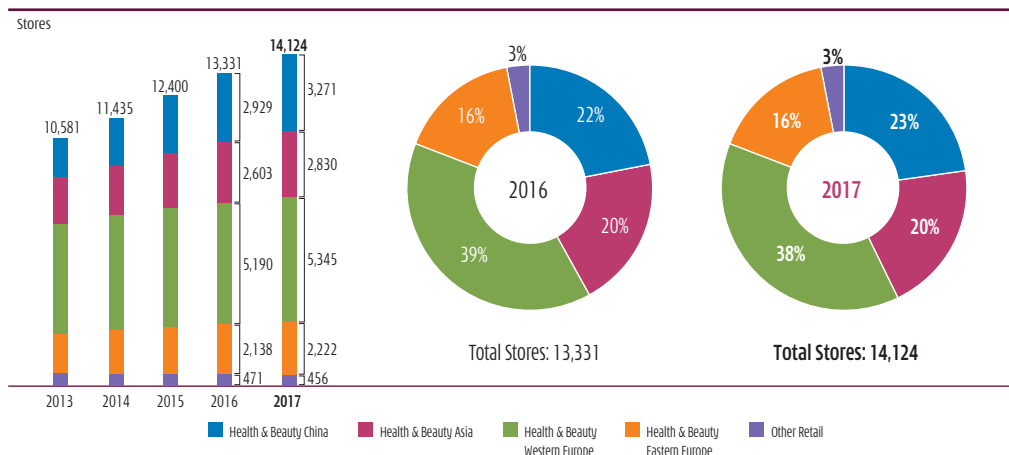
Note 1: Other Retail includes PARKNSHOP, Fortress, Watson's wine and manufacturing operations for water and beverage businesses.

Note 2: Comparable stores sales growth represents the percentage change in revenue contributed by stores which, as at the first day of the relevant financial year (a) have been operating for over 12 months and (b) have not undergone major resizing within the previous 12 months.

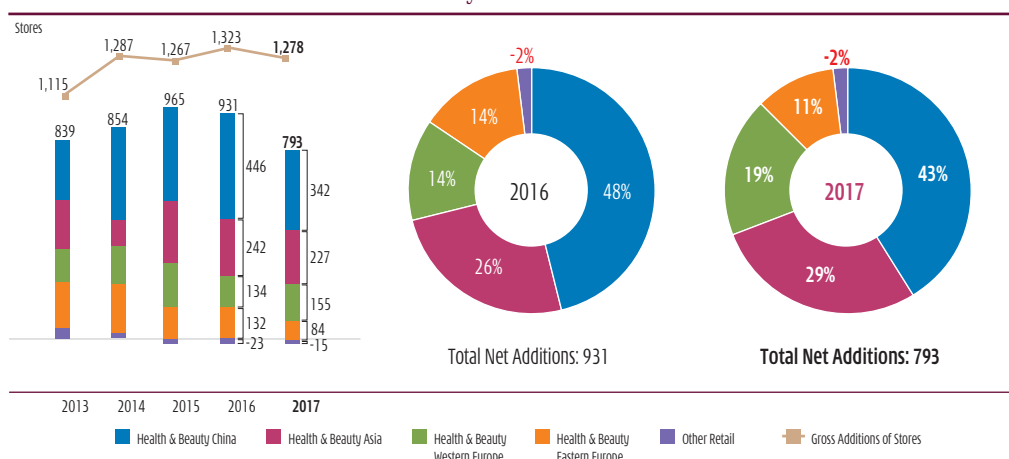
Note 3: Adjusted for the CRM sales recovered in the new stores opened in proximity, comparable stores sales grew by 0.3% instead of a decline of 4.3% in 2017 (2016: comparable stores sales declines reduced from 10.1% to 5.0%).

Group Performance (continued)

**Total Retail Store Numbers
by Subdivision**



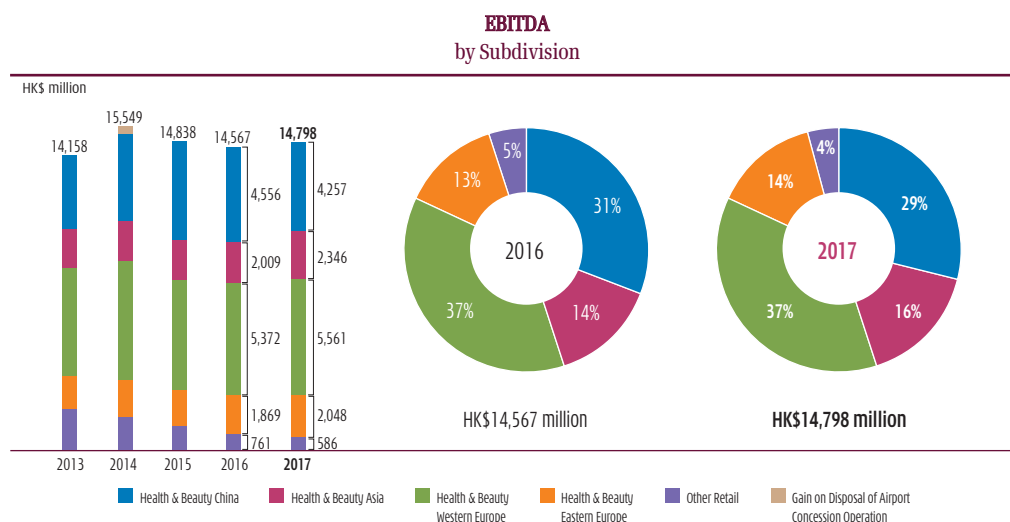
**Total Net Additions of Retail Store
by Subdivision**



Store Numbers	2017	2016	Change
Health & Beauty China	3,271	2,929	+12%
Health & Beauty Asia	2,830	2,603	+9%
Health & Beauty China & Asia Subtotal	6,101	5,532	+10%
Health & Beauty Western Europe	5,345	5,190	+3%
Health & Beauty Eastern Europe	2,222	2,138	+4%
Health & Beauty Europe Subtotal	7,567	7,328	+3%
Health & Beauty Subtotal	13,668	12,860	+6%
Other Retail ⁽¹⁾	456	471	-3%
Total Retail	14,124	13,331	+6%

Note 1: Other Retail includes PARKnSHOP, Fortress, Watson's Wine and manufacturing operations for water and beverage businesses.

The retail division's EBITDA increased by 2% but EBIT remained flat in reported currency against 2016. Revenue growth in the Health and Beauty segment was partly offset by higher operating costs associated with the store portfolio expansion, as well as lower contribution from Other Retail operations. The EBITDA improvements were largely offset by the higher depreciation charge from the expansion of stores and investments in system enhancement and development for data management and e-commerce platforms.



EBITDA	2017 HK\$ million	2016 HK\$ million	Change	Change in Local Currency
Health & Beauty China	4,257	4,556	-7%	-6%
Health & Beauty Asia	2,346	2,009	+17%	+16%
Health & Beauty China & Asia Subtotal	6,603	6,565	+1%	+1%
Health & Beauty Western Europe	5,561	5,372	+4%	—
Health & Beauty Eastern Europe	2,048	1,869	+10%	+3%
Health & Beauty Europe Subtotal	7,609	7,241	+5%	+1%
Health & Beauty Subtotal	14,212	13,806	+3%	+1%
Other Retail ⁽¹⁾	586	761	-23%	-23%
Total Retail	14,798	14,567	+2%	—

Note 1: Other Retail includes PARKnSHOP, Fortress, Watson's Wine and manufacturing operations for water and beverage businesses.

The overall health and beauty subdivision, which represented 96% of the division's EBITDA, continued to deliver healthy performances in 2017 with a reported EBITDA growth by 3%. In particular, Health and Beauty Asia reported a 17% EBITDA growth supported by an improved EBITDA margin. The health and beauty subdivision continued to expand its portfolio with 808 net addition of stores. The quality of new store openings remains high with an average new store cash payback period of 11 months. The average capex per new store for the health and beauty subdivision was HK\$0.9 million.

Segment Performance

Health and Beauty China

	2017 HK\$ million	2016 HK\$ million	Change	Change in Local Currency
Total Revenue	21,783	20,914	+4%	+5%
EBITDA <i>EBITDA Margin %</i>	4,257 20%	4,556 22%	-7%	-6%
EBIT <i>EBIT Margin %</i>	3,674 17%	4,055 19%	-9%	-8%
Total Store Numbers	3,271	2,929	+12%	
Comparable Stores Sales Growth (%)	-4.3%	-10.1%		

The Watsons business continued to be the leading health and beauty retail chain in the Mainland. Total revenue increased by 4% with a 12% increase in store numbers, partly offset by a negative 4.3% comparable stores sales decline in mature stores. With various initiatives, including store segmentation, refit and re-layout, comparable store sales decline gradually improved from a negative 10.1% for 2016 to negative 4.3% for 2017, and returned to marginal positive 0.1% comparable store sales growth in the last quarter. Through continuous expansion of store portfolio which also follows closely with shifts of trade zones and customer demographics, sales declines in mature stores during 2017 were fully recovered in new stores opened in the proximity of such mature stores. Recovery of sales is measured by tracking the operation's extensive CRM customer base sales performances. Taking into account the CRM sales recovery, the comparable stores sales growth is 0.3 % for 2017.

Despite the revenue growth, both EBITDA and EBIT declined by 6% and 8% in local currency respectively in 2017 mainly due to higher inflation resulting in higher overall store operating cost base. However, EBITDA margin remained strong at 20%.

Health and Beauty China increased its total number of stores by 342 during the year with an average new store cash payback period of 10 months and had more than 3,200 stores operating in 454 cities in the Mainland as at year end.

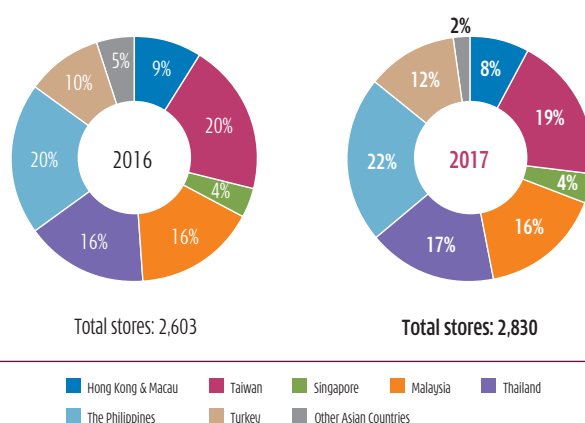
Health and Beauty Asia

	2017 HK\$ million	2016 HK\$ million	Change	Change in Local Currency
Total Revenue	25,154	23,814	+6%	+6%
EBITDA <i>EBITDA Margin %</i>	2,346 9%	2,009 8%	+17%	+16%
EBIT <i>EBIT Margin %</i>	1,955 8%	1,643 7%	+19%	+18%
Total Store Numbers	2,830	2,603	+9%	
Comparable Stores Sales Growth (%)	+3.8%	+1.9%		

Watsons is the leading health and beauty retail chain in Asia with strong brand name recognition and extensive geographical coverage. The majority of its businesses in this region reported strong performances, particularly Watsons Thailand, Malaysia and Philippines. Watsons Hong Kong reported a double digit increment in both EBITDA and EBIT despite the pressure from lower tourist arrivals in the first half of the year and higher operating costs in Hong Kong.

Health and Beauty Asia increased its total number of stores by 227 during the year achieving an average new store cash payback period of 13 months. The subdivision had more than 2,800 stores operating in 9 markets in 2017.

Health and Beauty Asia (+9%)
Number of Retail Stores by Market



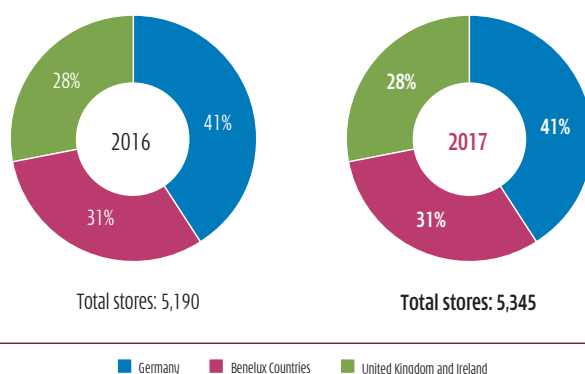
Health and Beauty Western Europe

	2017 HK\$ million	2016 HK\$ million	Change	Change in Local Currency
Total Revenue	64,523	61,584	+5%	+3%
EBITDA	5,561	5,372	+4%	—
<i>EBITDA Margin %</i>	9%	9%		
EBIT	4,543	4,428	+3%	-1%
<i>EBIT Margin %</i>	7%	7%		
Total Store Numbers	5,345	5,190	+3%	
Comparable Stores Sales Growth (%)	+2.1%	+3.7%		

Health and Beauty Western Europe continued to report good revenue growth in both reported and local currencies during the year. Health and Beauty UK, continued its improved performance with a healthy comparable stores sales growth of 3.2% in 2017, while the Benelux countries experienced intense competition resulting in slightly lower contributions despite sales growth running above market levels in 2017.

Health and Beauty Western Europe added 155 stores and operated more than 5,300 stores in 2017. The average new store cash payback period of this subdivision was 11 months.

Health and Beauty Western Europe (+3%)
Number of Retail Stores by Market



Segment Performance (continued)

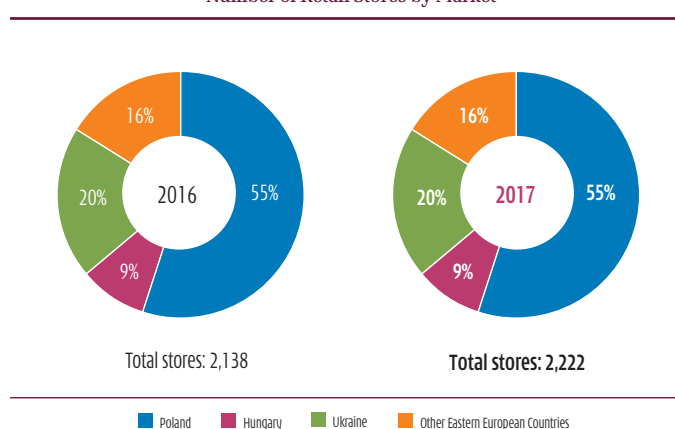
Health and Beauty Eastern Europe

	2017 HK\$ million	2016 HK\$ million	Change	Change in Local Currency
Total Revenue	14,866	13,076	+14%	+7%
EBITDA	2,048	1,869	+10%	+3%
<i>EBITDA Margin %</i>	<i>14%</i>	<i>14%</i>		
EBIT	1,785	1,623	+10%	+3%
<i>EBIT Margin %</i>	<i>12%</i>	<i>12%</i>		
Total Store Numbers	2,222	2,138	+4%	
Comparable Stores Sales Growth (%)	+4.4%	+4.6%		

Health and Beauty Eastern Europe continued to report healthy growth during the year. The 10% growth in both EBITDA and EBIT was mainly attributable to strong sales of the Rossmann joint venture in Poland.

Health and Beauty Eastern Europe added 84 stores and operated more than 2,200 stores in 7 markets in 2017.

Health and Beauty Eastern Europe (+4%)
Number of Retail Stores by Market



Other Retail

	2017 HK\$ million	2016 HK\$ million	Change	Change in Local Currency
Total Revenue	29,837	32,114	-7%	-7%
EBITDA	586	761	-23%	-23%
<i>EBITDA Margin %</i>	2%	2%		
EBIT	131	311	-58%	-58%
<i>EBIT Margin %</i>	1%	1%		
Total Store Numbers	456	471	-3%	
Comparable Stores Sales Growth (%)	-2.3%	-8.2%		

Other Retail subdivision, which only represented 4% of the division's EBITDA, reported lower total revenue, EBITDA and EBIT which declined by 7%, 23% and 58% respectively, mainly due to cost inflation and stagnant visitor consumption. Encouragingly, a pickup of tourist arrivals was seen in the second half of the year and positive sales growth momentum was reported by the Hong Kong Operations, particularly Fortress. Other Retail currently operates over 450 retail stores in 3 markets, as well as manufactures and distributes bottled water and other beverages in Hong Kong and the Mainland.

Other Retail (-3%)
Number of Retail Stores by Segment

