MANAGEMENT DISCUSSION AND ANALYSIS

INDUSTRY REVIEW

In 2019, the world economy showed signs of recovery yet the rebound is still masked with uncertainties. As for the PRC, it picked up GDP growth rate gradually after 6 years of declining speed. While the PRC is developing and reforming on its path of economic new normal, domestic demand and consumer market pose more and more importance to its future growth.

Information from the National Bureau of Statistics of China indicates that per capita disposable income in the PRC in 2019 was RMB30,733, representing an increase of 8.9% as compared with that of last year. Per capita consumption expenditure also increased 8.6% to RMB21,559, while the Engel coefficient, i.e. the proportion of income spent on food, continued to fall, indicating an increasing living standard in the country.

After rapid growth in previous two decades, the PRC has become the largest home furniture production base and exporter. With the growing wealth of the PRC population, people are more willing to purchase and replace home furnishing products. However, the home furnishing manufacturers in the PRC are much less concentrated than in other industries, posing pressures on many of the market players.

BUSINESS REVIEW

China Creative Global is principally engaged in the business of design, development, manufacture and sales of home decor products and electric fireplaces. The Group sells its products domestically in the PRC under its "Allen"(亚伦) brand and export its products on ODM/OEM basis to countries including the U.S., Germany, Canada, France and the U.K..

The revenue of the Group for the year ended 31 December 2019 decreased by 24.5% to RMB115.2 million from RMB152.5 million for the year ended 31 December 2018. The loss attributable to the equity holders of the Company was RMB1,676.0 million, representing an increase of 1,048.7% as compared to the loss of RMB145.9 million for the year ended 31 December 2018. This was mainly due to (1) increases in selling and distribution expenses, and administrative and other operating expenses; and (2) the net loss arising on deconsolidation of subsidiaries of RMB1,329.1 million.

The Group's products are under two major categories, namely (1) electric fireplaces and (2) home decor products. Revenue distribution by the two categories for the year ended 31 December 2019 were 61.3% and 38.7% respectively, while the proportions were 69.4% and 30.6% respectively last year.

During the year ended 31 December 2019, overseas market contributed RMB81.6 million (2018: RMB85.6 million), or 70.8% (2018: 56.1%) to the Group's total revenue. Revenue from the PRC market decreased from RMB66.9 million in the year ended 31 December 2018 to RMB33.6 million in the year ended 31 December 2019, taking up 29.2% (2018: 43.9%) of the total revenue.

The Group considers innovation as the core element of its development. The design team consists of 39 staff as at 31 December 2019.

DECONSOLIDATION OF SUBSIDIARIES LOST CONTROL

As noted in the Company's announcement dated 7 May 2021, the PRC subsidiaries held by Allen International Holdings Limited ("Allen International"), namely Allen Electronics Co., Ltd. Fujian (福建亞倫電子電器科技有限公司), Allen China Co., Ltd. (亞倫(中國)有限公司) and Quanzhou Allen Light Industry Co., Ltd. (泉州亞倫輕工有限公司) (the "Deconsolidated Subsidiaries") were transferred to 泉州大東敏盛健康發展有限公司 on 20 November 2020, without any prior approval or notice to the Company's Board of Directors and, being the transfer of the Company's substantial assets, without approval by the Company's Shareholders. The Company has set up an Investigation Committee to study and take actions against these transfers and this Committee has then appointed Manivest Asia Limited ("Manivest") to conduct investigations in these respect. Upon the First Report produced by Manivest, it was noted that the Company has already lost of the controlling in the subsidiaries as at 31 December 2019 and hence, the Group no longer consolidated the financial position and performance of the Deconsolidated Subsidiaries starting from 31 December 2019. The deconsolidation had resulted in a net loss on deconsolidation of subsidiaries of approximately RMB1,329.1 million as the directors were of the view that the recoverability of the amounts due from Deconsolidated Subsidiaries was remote and do not expect to be able to recover the outstanding balances in the foreseeable future.

FINANCIAL ANALYSIS

Revenue

Our revenue decreased by RMB37.3 million from RMB152.5 million to RMB115.2 million, represented a decrease of 24.5% compared with last year. The decrease was mainly driven by the lower market demand.

Revenue analysis by product type is as follows:

	2019		2018	
	RMB'000	**% of revenue**	RMB'000	% of revenue
Electric fireplaces				
Frame electric fireplaces	**7,436**	**6.5**	13,077	8.6
Non-framed electric fireplaces	**10,948**	**9.5**	15,086	9.9
Heater and others	**52,242**	**45.3**	77,619	50.9
	70,626	**61.3**	105,782	69.4
Home decor products				
Polyresin series	**44,597**	**38.7**	46,719	30.6
	115,223	**100**	152,501	100

The decrease in the sales of electric fireplaces and home decor products was primarily due to the decrease in sales volume due to the lower market demand in the PRC.

Gross Profit And Gross Profit Margin

Our gross profit increased from RMB17.7 million for the year ended 31 December 2018 to RMB31.8 million for the year ended 31 December 2019, represented an increase of 79.7% compared with last year mainly due to the increase in gross profit margin.

The gross profit margin increased from 11.6% for the year ended 31 December 2018 to 27.6% for the year ended 31 December 2019. The increase was primarily due to the increase in average selling prices.

Other Income

Other income decreased by RMB2.0 million or approximately 16.4%, from RMB12.2 million for the year ended 31 December 2018 to RMB10.2 million for the year ended 31 December 2019 primarily due to the decreases in interest income and rental income.

Other Gains Or (Losses) — Net

The Group's other gains or losses mainly consists of loss on disposal/write-off of property, plant and equipment of RMB1.3 million and set off by the net foreign exchange gain of RMB1.5 million for the year ended 31 December 2019. The Group's other losses mainly consists of the net foreign exchange loss of RMB2.8 million and loss on disposal/write-off of property, plant and equipment of RMB19.6 million for the year ended 31 December 2018.

Selling And Distribution Expenses

Our selling and distribution expenses increased by RMB205.3 million, or approximately 11.9 times, from RMB17.2 million for the year ended 31 December 2018 to RMB222.5 million for the year ended 31 December 2019 primarily due to the increase in advertising and promotion expenses to enhance the brand recognition of "Allen (亚伦)" and to increase our market share in the PRC.

Administrative And Other Operating Expenses

Our administrative and other operating expenses increased by RMB67.2 million, or approximately 99.7%, from RMB67.4 million for the year ended 31 December 2018 to RMB134.6 million for the year ended 31 December 2019. The increase was mainly due to (1) the bonus payment of RMB18.0 million to the senior management of the Group for their contribution to our Group for the Year 2016 to the first half of the Year 2019; (2) the technical services provided by an university of RMB7.8 million incurred; (3) compensation paid of RMB19.7 million for the removal of premises on our factories disposed of; and (4) charitable donations of RMB23.5 million to the local government.

Impairment Losses on Property, Plant And Equipment

As at 31 December 2018, the Group had property, plant and equipment of approximately RMB401.5 million and RMB211.4 million located in Anhui and Quanzhou, the PRC respectively. For the year ended 31 December 2018, the Group's operation in Anhui and Quanzhou have been making losses and management has performed an impairment assessment, taking into account the current status of the assets and market price/transactions for similar assets. Based on the result of the assessment, carrying amount of the property, plant and equipment in Anhui and Quanzhou is lower than its recoverable amount, and therefore, an impairment provision of RMB10.8 million has been made during the year.

In 2019, these assets are under deconsolidation and fully written off accordingly.

Finance Costs

The Group's finance costs increased by RMB3.7 million, or approximately 18.3%, from RMB20.2 million for the year ended 31 December 2018 to RMB23.9 million for the year ended 31 December 2019. The increase was mainly due to the increase in interest expenses and set off by the decrease in the foreign exchange loss arising from borrowings denominated in HKD.

Income Tax Expenses

Our income tax expenses remained the same at RMB0.8 million for the years ended 31 December 2018 and 2019.

Loss for The Year Attributable To Owners Of the Company

Loss attributable to owners of the Company was approximately RMB1,676.0 million, an increase of 1,048.7% from approximately RMB145.9 million last year. The increase in loss was primarily due to (i) the net loss arising on deconsolidation of subsidiaries of approximately RMB1,329.1 million (2018: Nil) and (ii) the increase of the Company's administrative and other operating expenses of RMB67.2 million and selling and distribution expenses of RMB205.3 million.

CAPITAL STRUCTURE, LIQUIDITY, FINANCIAL AND CAPITAL RESOURCES

	2019	2018
Current ratio(1)	**0.0**	7.1
Gearing ratio (%)(2)	**N/A**	8.6%

(1) Current ratio is calculated based on our total current assets divided by our total current liabilities.

(2) Gearing ratio calculated based on our total debts (being our bank borrowings) divided by our total equity.

FOREIGN EXCHANGE RISK

Our functional currency is RMB. Our Group's foreign exchange risk mainly relate to fluctuations in exchange rates of RMB against our bank balances in USD and HKD and trade receivables denominated in USD, and these may affect our operation results. Our Group does not have a hedging policy. However, our management monitors foreign exchange exposure and will consider hedging significant foreign currency exposure should the need arise.

USE OF PROCEEDS FROM GLOBAL OFFERING

The Shares of the Company were listed on the Main Board of the Stock Exchange on 20 December 2013. Net proceeds from the global offering were approximately HK$597.2 million (after deducting the underwriting commission and relevant expenses). As at 31 December 2019, the unused proceeds were deposited in licensed banks in Hong Kong and the PRC.

	Percentage to total amount	Net Proceeds HK$' million	Utilised Amount as at 31 December 2019 HK$' million	Unutilised Amount as at 31 December 2019 HK$' million
Establishing new production facilities	53.7%	**320.7**	**320.7**	**—**
Establishing seven creative home furnishing concept shops	16.0%	**95.6**	**36.8**	**58.8**
Expanding overseas sales network under our own brand overseas	7.3%	**43.6**	**13.2**	**30.4**
Own-brand promotion	7.0%	**41.8**	**41.8**	**—**
Increasing and enhancing our research and development activities	6.0%	**35.8**	**35.8**	**—**
General working capital	10.0%	**59.7**	**59.7**	**—**
		597.2	**508.0**	**89.2**

EMPLOYEES AND EMOLUMENTS

As at 31 December 2019, we employed a total of 411 full time employees in the PRC and Hong Kong which included management staff, product designers, technicians, salespersons and workers. For the year ended 31 December 2019, the Group's total expenses on the remuneration of employees was RMB59.8 million, representing 51.9% of the revenue of the Group.

Our emolument policies are formulated based on the performance of individual employee which will be reviewed periodically. Apart from the provident fund scheme (operation in accordance with the provisions of the Mandatory Provident Fund Schemes Ordinance for Hong Kong employees) or social insurance fund (including retirement pension insurance, medical insurance, unemployment insurance, injury insurance and maternity insurance for the PRC employees), discretionary bonuses and employee share options are also awarded to employees according to the assessment of individual performance. Since the adoption of the share option scheme on 2 December 2013 and up to 31 December 2019, no options have been granted.

CAPITAL EXPENDITURE

For the year ended 31 December 2019, the capital expenditure of the Group amounted to RMB0.2 million. It was mainly comprised of property, plant and equipment.

MATERIAL ACQUISITION AND DISPOSALS AND SIGNIFICANT INVESTMENTS

The Group did not have any material investments or capital assets, or material acquisitions or disposals of subsidiaries or significant investments for the year ended 31 December 2019.

CONTINGENT LIABILITIES

As at 31 December 2019, the Group did not have any significant contingent liabilities.

PURCHASES, SALE OR REDEMPTION OF LISTED SECURITIES

The Company has not redeemed any of the shares of the Company during the year ended 31 December 2019. Neither the Company nor any of its subsidiaries had purchased or sold any of the Company's securities during the year ended 31 December 2019.

COMPLIANCE WITH THE CORPORATE GOVERNANCE CODE

The Company was committed to maintaining high level of corporate governance and has steered its development and protected the interests of its shareholders in an enlightened and open manner. The Board comprises seven executive Directors and four independent non-executive Directors. The Board has adopted the code provisions of the Corporate Governance Code (the "Code Provisions") set out in Appendix 14 to the Rules Governing the Listing of Securities on the Stock Exchange (the "Listing Rules"). The Board has instructed to perform a review to the compliance of the Corporate Governance Code for the preceding year and the reporting year 2019. The Board has adopted the results and the recommendations from this review and improved the compliance on the Code Provisions.

MODEL CODE FOR SECURITIES TRANSACTIONS BY DIRECTORS

The Company has adopted the Model Code for Securities Transactions by Directors of Listed Issuers contained in Appendix 10 to the Listing Rules (the "Model Code") as its own code of conduct for dealing in securities of the Company by the Directors. Specific enquiries have been made with the Directors, and all Directors confirmed in writing that they have complied with the required standards set out in the Model Code regarding their securities transactions for the year ended 31 December 2019.

MANAGEMENT DISCUSSION AND ANALYSIS

ADDRESSING ALL CONCERNS RAISED BY THE COMPANY'S AUDITORS

In the audited report of the Company for the year ended 31 December 2019, the Company's auditors issued disclaimer of opinion in the following matters, please refer to the auditor's report for full explanation:

1. **Deconsolidation of subsidiaries and material uncertainties relating to the forensic investigation from special investigation committee of the Company**

   As noted above, the Company's subsidiaries held under Allen International were illegally transferred. Deconsolidation of the subsidiaries has to be adopted for accounting purposes. In addition, due to the absence of complete accounting books and records of the Deconsolidated Subsidiaries, the Company's auditors are unable to obtain sufficient appropriate audit evidence to satisfy themselves about the occurrence, completeness, accuracy, cut-off, classification and presentation and related disclosure of the results and related party transactions of the Deconsolidated Subsidiaries for period from 1 January 2019 to 31 December 2019. In addition, due to circumstances described above, the Company's auditor is unable to obtain sufficient appropriate audit evidence and explanations as to whether the contingent liabilities and commitments committed by the Group were properly recorded and accounted for. There were no alternative audit procedures that the Company's auditors could perform to satisfy themselves as to whether the contingent liabilities and commitments were free from material misstatements.

   The Company has initiated legal actions against the holding company of the PRC entity acquiring the subsidiaries. In addition, the Company has instructed a PRC lawyer to take investigations in respect of the Deconsolidated Subsidiaries and to take actions to regain controls and ownership in the Deconsolidated Subsidiaries. In addition, in order to address the concerns raised by the auditors of the Company, the directors of the Company will continue to consult legal opinion on possible further steps. Further announcement(s) will be made by the Company as and when appropriate to keep the shareholders informed of the material developments in the above matters.

   In order to identify the internal control weaknesses which may directly or indirectly have led to the illegal transfer of the Deconsolidated Subsidiaries mentioned above, the Company's management has instructed the Internal Control Manager to review the Company's internal control policies and procedures for the preceding years and the year concerned and report to the Company's audit committee. These weaknesses are then confirmed and recognised by the management and thereafter rectified or modified by new internal control policies and procedures.

2. **Multiple uncertainties relating to going concern**

   In view of the outstanding bond borrowings amounting to RMB139.4 million as at 31 December 2019 and other payables not settled;(ii) the processing of the Company's restructuring; and (iii) the Group's net loss attributable to the owners of the Company of approximately RMB1,676.0 million during the year ended 31 December 2019 and net liabilities of approximately RMB152.8 million as at 31 December 2019, the Company's auditors considered these indicate the existence of material uncertainties that may cast significant doubt on the Group's ability to continue as a going concern.

To maintain the ongoing of the Company, the management has introduced Gold Future Industrial Limited to the Group. In addition, there may have more potential acquisitions or joint ventures to be setup soon, as the negotiations are in the final stage now.

Based on the above and subject to the successful restructuring and resumption of the Company, the management strongly believes that the going concern matters will be solved, as these businesses activities shall produce significant incomes and profits to maintain the Company's survival and ongoing operations.

3. Scope limitation of trade and other payables and current tax liabilities

The management considers that the trade and other payables of RMB2,000,000 and current tax liabilities of RMB3,671,000 are brought forward from preceding years. The trade and other payables should be in respect of the subsidiary company which has ceased operations and current tax liabilities may represent the under-provisions of tax in respect of the payments of interest expenses calculated on the inter-company balances due from 亞倫福建電子 to Allen International. Due to loss of control over the Deconsolidated Subsidiaries, the current directors cannot obtain sufficient information in respect of the above balances.

The management shall consider to obtain further steps/information to clear and dispose of this qualification in future.

4. Opening balances and corresponding figures

Due to the loss of control in the Company's subsidiaries, the opening balances are disclaimed for the year ended 31 December 2019.

FINAL DIVIDENDS

The Board does not recommend the payment of a final dividend for the year ended 31 December 2019 (2018: Nil).