

# Enterprise Risk Management Report

Effective risk management is essential to the achievement of the Group's strategic objectives. In place since 2010, the Group's ERM system offers a systematic and disciplined approach to provide clear responsibility and accountability structures for risk management. It consists of three major components: risk governance; risk infrastructure and oversight; as well as assignment of risk ownership.

The Board is responsible for determining the Group's risk profile and risk appetite, with the latter defining the acceptable tolerance levels for key risks. The Board oversees the Group's risk management framework, reviews the Group's key existing and potential risks and their respective mitigation strategies, and ensures risk management effectiveness.

## Risk Management Committee

The Group formed the Risk Management Committee ("RMC") in 2009 that comprises three Executive Directors as part of the Group's commitment to further enhancing our control environment. The RMC has written terms of reference that set out the responsibilities of the members, which are available on the Company's website. The RMC assists the Board in providing leadership to the management in relation to risk management and internal control. The RMC has overall responsibility for the establishment and maintenance of an appropriate and effective risk management and internal control systems including the design, implementation and monitoring of such systems for the Group. For the year ended 31 March 2021, the Committee held two meetings to assess and re-assess the major risks and to review the management of these risks and the effectiveness of mitigation actions, while also actively identifying any positive business opportunities that arise in relation to these risks.

## Enterprise Risk Assessment

Risk assessment is the identification and analysis of existing and emerging risks in order to form a basis for determining how risks are managed in terms of likelihood and impact. Risk areas are categorised into strategic, operational, financial and compliance perspectives for further assessment and management. A bottom-up and top-down approach is adopted to ensure a holistic risk management process, and a risk register has been maintained since the inception of the ERM system. This register has been regularly monitored and updated by taking emerging risks into account for continuous risk assessment purposes and building the risk-based internal audit plan.

The Group has in place the Control Self-Assessment, requiring all business units and major departments in the headquarters to annually assess the adequacy and effectiveness of risk management and internal control, as well as to identify potential and significant risks.

## Enterprise Risk Management Process

The ERM system uses risk indicators to monitor major risks. The setting of risk indicators aligns with the risk tolerance regime, representing the magnitude of risk the Group is willing to undertake in order to achieve its business goals. Risk owners are required to take mitigating actions to address these risks. Such actions are integrated into the Group's day-to-day activities while their effectiveness is closely measured by risk indicators. This system is used as a basis for reporting and discussion in the management meetings as well as in RMC meetings. If any risk indicators underperformed, the responsible risk owners are required to re-assess the existing remedial action plans and promptly propose new plans if necessary.

Members of the RMC meet as often as necessary to review and discuss the risk management progress of each of the major risks and to provide a continuous update on the business environment and to monitor any changes. The IAMS Department carries out continuous assessment on the progress of risk management procedures while it also evaluates the risk responses submitted by risk owners. The IAMS Department facilitates the RMC in reporting significant risks, material changes and the associated mitigating actions to the Audit Committee on a quarterly basis.

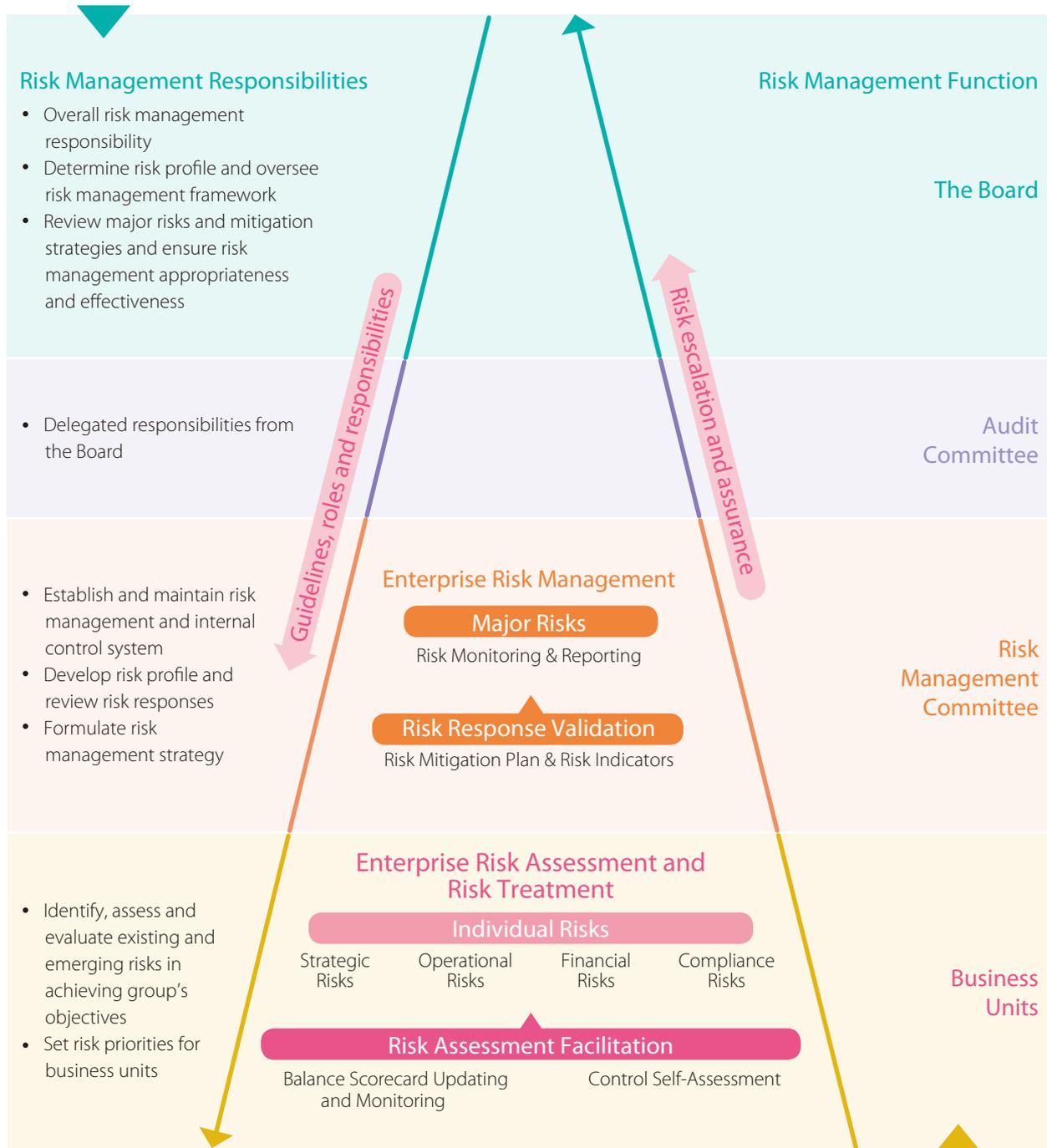
The balance scorecard system has been implemented, with the incorporation of key performance indicators for major departments in headquarters to measure their progress towards achieving business goals. During the year, we started to align the reporting of the balance scorecard system and the ERM system to provide management with a comprehensive set of indicators for monitoring both business performance and risks. An illustrative diagram describing our ERM framework is set out on page 82.

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## Risk Governance & Infrastructure

### The ERM Framework

#### Top Down Approach



#### Bottom Up Approach

## Management of Major Risks

There have been no significant changes in the nature and extent of major risks during the year. We recognise that market concentration risk, online threats and opportunities and product competitiveness remain the major risks that the Group has to manage amid the economic downturn brought about by the COVID-19 pandemic.

### Market Concentration Risk

Brick-and-mortar business has historically been the main focus of the Group in all markets, and mainland tourists have made up a substantial proportion of our sales in our core markets of Hong Kong and Macau SARs, accounting for more than 60% of their turnover over the past few years. Since the outbreak of COVID-19 in early 2020, the Hong Kong and Macau SARs governments have implemented stringent border control measures for inbound travellers which brought tourist arrivals to a standstill and curtailed the entire retail industry. In addition, our sales in physical stores have been affected by the increasing pace at which consumers are moving towards online purchases.

The Group has adopted a diversification strategy in terms of sales channels and markets, customers and products to alleviate this market concentration risk and has further expanded our online business in line with the latest development and trend to balance its mix of online and offline operations (for details, please refer to the Online Threats and Opportunities section). The Group is also accelerating its penetration into the Mainland China market as an effort to balance its geographical sales mix from brick-and-mortar stores (for details, please refer to the Mainland China and Malaysia Business Prospects section).

During the year, the Group stepped up its efforts in serving local consumers in Hong Kong and Macau SARs markets. We have offered extensive range and large volume of protective and personal care products from the start of the pandemic (for details, please refer to the Product Competitiveness section). We have also launched aggressive promotional activities to attract local customers and sourced more personal care products to accommodate their needs. Furthermore, the Group will develop customer experience zones in designated physical stores to deliver more personal services and exclusive in-store experiences.

### Online Threats and Opportunities

The COVID-19 pandemic has accelerated the purchase behaviour shift towards online shopping. We are further developing our online touch points and increasing the coordination of our online and offline product offerings and fulfilment with the aim of providing a seamless shopping experience which will enable us to interact with and serve our customers irrespective of where they are.

Sales through third-party platforms represent a significant part of our sales. We are strategically committed to extending our reach beyond Mainland China and are collaborating with current and targeting other well-known e-commerce platforms to serve different markets in Asia.

Recognising that the role of physical stores is changing in the new retail era. The Group will invest more resources in expanding online business and take full advantage of our physical stores by accelerating the collaboration of online platforms and offline store network, with a view to providing customers with a seamless O2O shopping experience in the future. To this end, digital marketing including social media and livestreaming are increasingly engaged to promote interaction with consumers.

We aim to incorporate and consolidate online and offline customer databases in the Hong Kong and Macau SARs markets and in time also the Mainland China market for the purpose of boosting customer loyalty and repurchase rate.

### Product Competitiveness

In a fast changing and increasingly competitive market, our continued success hinges on our ability to strengthen our house brands while sourcing and developing products that meet the rapidly evolving demand.

Our product offering traditionally focuses mostly on skincare, makeup and fragrances. As the pandemic has caused significant changes in consumers' product needs, we have responded by introducing popular product categories including protective products, and personal care products. We will focus on addressing the needs of our customers by tracking the latest market trends and continuously improve the attractiveness and competitiveness of our products.

Product category diversification will also address the limitations of a relatively narrow product offering that would see large fluctuations in sales performance. By adopting a more diversified product offering, we can improve the loyalty of existing customers, and attract new customers and customer segments.

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## Liquidity Risk

Working capital management is crucial to the sustainability of a company. The pandemic has led to a plunge in revenue in our core markets, significant losses and a drain on the Group's cash reserves. We have made great efforts to optimise our cost structure and exercise strenuous inventory management, in addition to exploring new revenue drivers.

## Cost Structure

This determines our profitability and ultimately our cashflow. We have been focusing our efforts on reducing staff costs and rental costs as they comprise the largest and second largest portion of the Group's expenses. Successful execution of the plan allows us to gain significant improvements in our profitability, competitiveness and liquidity. For staff costs, we have enforced the clearance of outstanding leave, implemented unpaid leave arrangements and temporary salary reduction schemes.

We have sought rental concessions and rental reductions upon renewal and have closed stores in tourist areas to reduce rental expenses and other physical store costs. The O2O business model also helps to lower expensive rents of physical stores. Ultimately, the aim is to rationalise store network and reduce store expenses to maximise store contribution, as well as to reduce non-productive costs to optimise our cost structure and therefore increase competitiveness and profitability.

## Inventory management

Inventory management plays a significant role in a company's liquidity since excessive inventories will tie up unnecessary funds and increase the risks of obsolescence. We succeeded in reducing excessive inventory by implementing aggressive clearance activities and placing stringent control on purchasing, and have allocated funds to strategically focused products only.

## Staff Health and Safety Risk

We recognise that human capital is one of the most important assets. Being a caring and socially responsible company, staff health, safety and livelihoods are always our primary concern. Since we are committed to providing a safe workplace for our employees, especially amid the COVID-19 crisis, the Group has developed and implemented measures to keep our employees safe (for details, please refer to the Environmental, Social and Governance Report – Protect Our Talents from COVID-19 section).

We continue to review the measures regularly and monitor notices issued by official sources while providing regular updates to our employees. We deeply believe that by always prioritising staff health and safety, we can keep our employees engaged and productive, retaining key talents and ensuring sustainability of our business.

## Cybersecurity and Personal Data Privacy Risks

Information technology has gained a higher strategic importance to achieving our objectives and is an increasingly weighted and integral part of our daily operations. We recognise that if technology-related risks are not adequately managed, they might negatively undermine our ability to meet the objectives that we are trying to achieve.

New retail operations require collection, processing and management of vast quantity of customer personal data from different legal jurisdictions that have been imposing ever more stringent regulations and penalties. As we aim to establish a centralised customer database for all our online and offline customers, we are exposed to personal data privacy risk that may result in losses to our customers, potential fines, as well as damage to our reputation and business. Cybersecurity and personal data privacy risks are thus together rated as a major risk to manage.

For that reason, the Group has been paying more attention to the information security management. An external consultant is engaged in conducting penetration testing annually and will be engaged whenever necessary to assure our effectiveness of information security. The Group has enhanced its existing IT security controls and implemented new measures to raise the staff awareness of potential IT security threats.

## Mainland China and Malaysia Business Prospects

The Mainland China and Malaysia markets have much more potential than we have exploited so far. Success in further penetration of these markets and their potential profit contribution will alleviate our market concentration risks.

In the Mainland China market, we are leveraging on the improving management team and product competitiveness to support the increasing pace of new store openings. The Group has strategically focused on the expansion of new stores in core city clusters to realise local management effectiveness and efficiency. In order to support the rapid business expansion, we will accelerate our progress in talent training, particularly in striving the better customer service and sales capabilities of frontline employees.

The Malaysian government issued Movement Control Orders, requiring mandatory temporary shop closures during different periods to contain the spread of the COVID-19 pandemic. The Group has responded to the unprecedented challenges by enhancing the product portfolio with protective and personal care products and introduction of online home delivery services. We established collaborative partnership with a number of online platforms during the year to allow customers to shop from home as well as to broaden our customer bases. The Group will remain prudent in store opening and continue to implement stringent cost reduction measures.

## Ethical Business Practice

We are committed to enforcing ethical business practice by setting the right tone at the top. However, we understand that unethical incidents may still happen even when we have a robust internal control system in place, especially when incentives or pressures to commit fraud increase significantly during economic downturn.

In order to enable us to evaluate and manage fraud risks through a more systematic approach, all business units and major departments in headquarters are required to formally assess and report annually their fraud risk exposure via the Control Self-Assessment. To proactively protect against fraud, we perform continuous monitoring of selected key operational processes for regions with high fraud vulnerability. All possible cases of fraud, either reported through the whistleblowing channel or identified by the analytics, will be conducted independently by the IAMS Department or jointly, if appropriate, with other departments in the Group or with external investigators. Prompt and consistent disciplinary actions will be taken according to company policy and the results, together with corrective actions to close the gaps and reduce the opportunity for fraudulent acts, will be reported to the Executive Directors and Audit Committee. Proper communication and training will be delivered thereafter to reduce the capacity for fraud. We believe that by so doing, we can safeguard our assets, contribute positively to our reputation and image, and thus reduce the direct and indirect costs of doing business.

## Third-Party Risks

The Group has been relying on third-party service providers, such as outsourced manufacturers, IT service providers, warehousing and logistics service providers in some key aspects of our business. Our aim is to improve performance by leveraging their specialised expertise, well-developed service network, operational efficiency and better scalability. Nevertheless, we are potentially exposed to risks that may include but are not limited to business disruptions, and reputational damage as a result of under-performance, non-compliance with local rules and regulations or unexpected withdrawal from the market of key service providers.

In order to counter these risks and make our business more secure, the Group has established comprehensive key performance indicators to continuously evaluate and monitor service levels. These measures may involve external professionals, executives and other functional teams for key projects as necessary, with clear terms and conditions laid out in service agreements. Although we tend to maintain long-term relationships with third-party service providers, we may terminate the services of under-performing vendors. In addition, from time to time we compare their service level and the price to that of the market, which allows us to bring in new vendors with better service quality and to update our backup vendor list while managing our costs.