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## THIS CIRCULAR IS IMPORTANT AND REQUIRES YOUR IMMEDIATE ATTENTION

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**If you are in any doubt** as to any aspect of this circular or as to the action to be taken, you should consult your licensed securities dealer, bank manager, solicitor, professional accountant or other professional adviser.

**If you have sold or transferred** all your shares in China Electronics Corporation Holdings Company Limited (the “Company”), you should at once hand this circular and the accompanying form of proxy to the purchaser or the transferee or to the bank, licensed securities dealer or other agent through whom the sale or transfer was effected for transmission to the purchaser or the transferee.

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### CHINA ELECTRONICS CORPORATION HOLDINGS COMPANY LIMITED

中國電子集團控股有限公司\*

*(Incorporated in the Cayman Islands and continued in Bermuda with limited liability)*

**(Stock Code: 00085)**

**MAJOR TRANSACTION AND CONNECTED TRANSACTION  
IN RELATION TO  
THE ACQUISITION OF A 95.64% EQUITY INTEREST IN HUAHONG  
CONTINUING CONNECTED TRANSACTIONS  
2015-2018 BUSINESS SERVICES AGREEMENT WITH CEC  
AND  
2015-2018 FINANCIAL SERVICES AGREEMENT WITH  
CEC FINANCE**

**Financial Adviser to the Company**



**Shenwan Hongyuan Capital (H.K.) Limited**

**Independent Financial Adviser to the Independent Board Committee and  
the Independent Shareholders**

**ALTUS CAPITAL LIMITED**

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A notice convening a special general meeting of the Company to be held at Plaza 1-2, Lower Lobby, Novotel Century Hong Kong, 238 Jaffe Road, Wanchai, Hong Kong on 19 November 2015 at 10:00 a.m. is set out on pages SGM-1 to SGM-4 of this circular. Whether or not you are able to attend the special general meeting, you are requested to complete the accompanying form of proxy in accordance with the instructions printed thereon and return the same to the Company's branch share registrar and transfer office in Hong Kong, Tricor Abacus Limited, at Level 22, Hopewell Centre, 183 Queen's Road East, Wanchai, Hong Kong not later than 48 hours before the time appointed for holding the special general meeting or any adjournment thereof. Completion and return of the form of proxy will not preclude you from attending and voting in person at the special general meeting or any adjourned meeting should you so wish.

A letter from the independent board committee of the Company containing its recommendation to the independent shareholders of the Company is set out on pages 41 to 42 of this circular. A letter from Altus Capital Limited, the independent financial adviser, containing its advice to the independent board committee and the independent shareholders of the Company is set out on pages 43 to 92 of this circular.

27 October 2015

\* For identification purpose only

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## DEFINITIONS

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*In this circular, unless the context otherwise requires, the following expressions have the following meanings:*

|                                          |                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                    |
|------------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| “2013-2016 Business Services Agreement”  | the 2013-2016 business services agreement dated 7 May 2013 and entered into between CEC and the Company                                                                                                                                                                                                                                                                                                                                                                                                            |
| “2015-2018 Business Services Agreement”  | the 2015-2018 business services agreement dated 26 June 2015 and entered into between CEC and the Company                                                                                                                                                                                                                                                                                                                                                                                                          |
| “2013-2016 Financial Services Agreement” | the comprehensive financial services agreement dated 7 May 2013 and entered into between the Company and CEC Finance                                                                                                                                                                                                                                                                                                                                                                                               |
| “2015-2018 Financial Services Agreement” | the comprehensive financial services agreement dated 26 June 2015 and entered into between the Company and CEC Finance                                                                                                                                                                                                                                                                                                                                                                                             |
| “Altus Capital”                          | Altus Capital Limited, a licensed corporation to conduct type 4 (advising on securities), type 6 (advising on corporate finance) and type 9 (asset management) regulated activities under the SFO, being the independent financial adviser to the Independent Board Committee and the Independent Shareholders in respect of the terms of the Shanghai Huahong Acquisition Agreements, the 2015-2018 Business Services Agreement and the 2015-2018 Financial Services Agreement and their respective proposed caps |
| “associates”                             | has the meaning ascribed to this term under the Listing Rules                                                                                                                                                                                                                                                                                                                                                                                                                                                      |
| “Board”                                  | the board of Directors                                                                                                                                                                                                                                                                                                                                                                                                                                                                                             |
| “CBRC”                                   | China Banking Regulatory Commission                                                                                                                                                                                                                                                                                                                                                                                                                                                                                |
| “CEC”                                    | China Electronics Corporation Limited (中國電子信息產業集團有限公司), a state-owned enterprise established under the laws of the PRC and the ultimate controlling shareholder of the Company                                                                                                                                                                                                                                                                                                                                     |

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## DEFINITIONS

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|-----------------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| “CEC Finance”                                 | China Electronics Financial Co., Ltd (中國電子財務有限責任公司), a company established under the laws of the PRC                                                                                                                                                                                                                                                                     |
| “CEC Group”                                   | CEC and its subsidiaries (other than the Group)                                                                                                                                                                                                                                                                                                                          |
| “CEC Technology”                              | China Electronics Technology Development Co., Ltd (中國電子科技開發有限公司), a company established under the laws of the PRC                                                                                                                                                                                                                                                        |
| “CEC Technology Financial Services Agreement” | the comprehensive financial services agreement dated 11 October 2013 and entered into between CEC Technology and CEC Finance                                                                                                                                                                                                                                             |
| “China Huada”                                 | China Integrated Circuit Design Corp., Ltd (中國華大集成電路設計集團有限公司), a company established under the laws of the PRC and a wholly-owned subsidiary of CEC and a substantial shareholder of the Company                                                                                                                                                                         |
| “Company”                                     | China Electronics Corporation Holdings Company Limited                                                                                                                                                                                                                                                                                                                   |
| “Completion”                                  | completion of the Huada Semiconductor Acquisition, the Individual Vendor Acquisition, the Huahong Group Acquisition and the Remaining Shareholders Acquisition in accordance with the terms of the Huada Semiconductor Agreement, the Individual Vendor Agreement(s), the Supplemental Huahong Group Agreement and the Remaining Shareholders Agreement(s), respectively |
| “connected person”                            | has the meaning ascribed to this term under the Listing Rules                                                                                                                                                                                                                                                                                                            |
| “Directors”                                   | the directors of the Company                                                                                                                                                                                                                                                                                                                                             |
| “Enlarged Group”                              | the Group immediately after the completion of the Shanghai Huahong Acquisition                                                                                                                                                                                                                                                                                           |
| “Group”                                       | the Company and its subsidiaries                                                                                                                                                                                                                                                                                                                                         |

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## DEFINITIONS

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|                                   |                                                                                                                                                                                    |
|-----------------------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| “HK\$”                            | Hong Kong dollars, the lawful currency of Hong Kong                                                                                                                                |
| “Hong Kong”                       | the Hong Kong Special Administrative Region of the PRC                                                                                                                             |
| “Huada Electronics”               | CEC Huada Electronic Design Co., Ltd (北京中電華大電子設計有限責任公司), a company established under the laws of the PRC and a wholly-owned subsidiary of the Company                              |
| “Huada Semiconductor”             | Huada Semiconductor Co., Ltd (華大半導體有限公司), a company established under the laws of the PRC and a wholly-owned subsidiary of CEC and a controlling shareholder of the Company        |
| “Huada Semiconductor Acquisition” | the acquisition of a 73.43% equity interest in Huahong by Huada Electronics from Huada Semiconductor pursuant to the Huada Semiconductor Agreement                                 |
| “Huada Semiconductor Agreement”   | the equity transfer agreement dated 26 June 2015 entered into between Huada Electronics and Huada Semiconductor in relation to the Huada Semiconductor Acquisition                 |
| “Huahong”                         | Shanghai Huahong Integrated Circuit Co., Ltd (上海華虹集成電路有限責任公司), a company established under the laws of the PRC                                                                     |
| “Huahong Group”                   | Shanghai Huahong (Group) Co., Ltd (上海華虹(集團)有限公司), a company established under the laws of the PRC and an associate of CEC                                                          |
| “Huahong Group Acquisition”       | the acquisition of a 7.62% equity interest in Huahong by Huada Electronics from Huahong Group pursuant to the Huahong Group Agreement and the Supplemental Huahong Group Agreement |
| “Huahong Group Agreement”         | the preliminary equity transfer agreement dated 26 June 2015 entered into between Huada Electronics and Huahong Group in relation to the Huahong Group Acquisition                 |

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## DEFINITIONS

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|----------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| “Independent Board Committee”    | the committee of Directors, which consists only of independent non-executive Directors, formed to advise the Independent Shareholders in respect of the terms of the Shanghai Huahong Acquisition Agreements, the 2015-2018 Business Services Agreement and the 2015-2018 Financial Services Agreement and their respective proposed caps |
| “Independent Shareholders”       | Shareholders other than CEC and its associates                                                                                                                                                                                                                                                                                            |
| “Individual Vendor(s)”           | the individual vendor(s) of the Individual Vendor Agreement(s) and/or the Remaining Shareholders Agreement(s), who are the director and/or employees of Huahong                                                                                                                                                                           |
| “Individual Vendor Acquisition”  | the acquisition of an aggregate of 9.95% equity interest in Huahong by Huada Electronics from the Individual Vendors pursuant to the Individual Vendor Agreement(s)                                                                                                                                                                       |
| “Individual Vendor Agreement(s)” | the equity transfer agreement(s) dated 26 June 2015 entered into between Huada Electronics and the respective Individual Vendor in relation to the Individual Vendor Acquisition                                                                                                                                                          |
| “Latest Practicable Date”        | 20 October 2015, being the latest practicable date prior to the printing of this circular for the purpose of ascertaining certain information for inclusion in this circular                                                                                                                                                              |
| “Listing Rules”                  | the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited                                                                                                                                                                                                                                                  |
| “Other Shareholders”             | being shareholders of Huahong holding an aggregate of 4.36% equity interest of Huahong who have not agreed to sell his or her respective equity interest in Huahong under the terms of the Shanghai Huahong Acquisition Agreements                                                                                                        |
| “PBOC”                           | the People’s Bank of China                                                                                                                                                                                                                                                                                                                |
| “PRC”                            | the People’s Republic of China                                                                                                                                                                                                                                                                                                            |
| “RMB” or “Renminbi”              | Renminbi, the lawful currency of the PRC                                                                                                                                                                                                                                                                                                  |

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## DEFINITIONS

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|-------------------------------------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| “Remaining Shareholders Acquisition”      | the acquisition of an aggregate of 4.64% equity interest in Huahong by Huada Electronics from the Individual Vendors pursuant to the Remaining Shareholders Agreement(s)                                                                                                                                            |
| “Remaining Shareholders Agreement(s)”     | the equity transfer agreement(s) dated 27 August 2015 entered into between Huada Electronics and the respective Individual Vendor in relation to the Remaining Shareholders Acquisition                                                                                                                             |
| “SFO”                                     | the Securities and Futures Ordinance (Chapter 571 of the Laws of Hong Kong)                                                                                                                                                                                                                                         |
| “SGM”                                     | the special general meeting of the Company to be convened to consider and, if thought fit, to approve (a) the Shanghai Huahong Acquisition and (b) the 2015-2018 Business Services Agreement and the 2015-2018 Financial Services Agreement and their respective proposed caps                                      |
| “SUAEE”                                   | the Shanghai United Assets and Equity Exchange                                                                                                                                                                                                                                                                      |
| “Shanghai Huahong Acquisition”            | together, the Huada Semiconductor Acquisition, the Individual Vendor Acquisition, the Huahong Group Acquisition and the Remaining Shareholders Acquisition                                                                                                                                                          |
| “Shanghai Huahong Acquisition Agreements” | together, the Huada Semiconductor Agreement, the Individual Vendor Agreement(s), the Huahong Group Agreement, the Supplemental Huahong Group Agreement and the Remaining Shareholders Agreement(s)                                                                                                                  |
| “Shareholder(s)”                          | shareholder(s) of the Company                                                                                                                                                                                                                                                                                       |
| “Shenwan”                                 | Shenwan Hongyuan Capital (H.K.) Limited, a licensed corporation to conduct type 1 (dealing in securities), type 4 (advising on securities) and type 6 (advising on corporate finance) regulated activities under the SFO, being the financial adviser to the Company in respect of the Shanghai Huahong Acquisition |

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## DEFINITIONS

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|----------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| “Stock Exchange”                       | The Stock Exchange of Hong Kong Limited                                                                                                                               |
| “Supplemental Huahong Group Agreement” | the supplemental equity transfer agreement dated 27 August 2015 entered into between Huada Electronics and Huahong Group in relation to the Huahong Group Acquisition |
| “%”                                    | per cent.                                                                                                                                                             |

*For ease of reference only, the names of PRC established companies and entities have been included in this circular in both Chinese and English and the English names of these companies and entities are either English translations of their respective official Chinese names or English trade names used by them. In the event of any inconsistency between the English names and their respective Chinese names, the Chinese names shall prevail.*

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## LETTER FROM THE BOARD

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### CHINA ELECTRONICS CORPORATION HOLDINGS COMPANY LIMITED

中國電子集團控股有限公司\*

(Incorporated in the Cayman Islands and continued in Bermuda with limited liability)

(Stock Code: 00085)

*Non-executive Directors:*

Rui Xiaowu (Chairman)

Dong Haoran

*Executive Directors:*

Liu Hongzhou (Vice Chairman)

Xie Qinghua (Managing Director)

*Independent Non-executive Directors:*

Chan Kay Cheung

Qiu Hongsheng

Chow Chan Lum

*Registered office:*

Clarendon House

2 Church Street

Hamilton HM 11

Bermuda

*Principal place of business  
in Hong Kong:*

Room 3403, 34th Floor

China Resources Building

26 Harbour Road

Wanchai

Hong Kong

27 October 2015

*To the Shareholders*

Dear Sir or Madam,

**MAJOR TRANSACTION AND CONNECTED TRANSACTION  
IN RELATION TO  
THE ACQUISITION OF A 95.64% EQUITY INTEREST IN HUAHONG**

**CONTINUING CONNECTED TRANSACTIONS  
2015-2018 BUSINESS SERVICES AGREEMENT WITH CEC  
AND  
2015-2018 FINANCIAL SERVICES AGREEMENT WITH  
CEC FINANCE**

**INTRODUCTION**

Reference is made to the announcements of the Company dated 28 June 2015 and 27 August 2015 in relation to, among other things, the entry into the Huada Semiconductor Agreement, the Individual Vendor Agreement(s), the Huahong Group Agreement, the Supplemental Huahong

\* For identification purpose only

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## LETTER FROM THE BOARD

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Group Agreement and the Remaining Shareholders Agreement(s) in respect of the Shanghai Huahong Acquisition. The aggregate consideration payable by Huada Electronics under the Huada Semiconductor Agreement, the Individual Vendor Agreement(s), the Supplemental Huahong Group Agreement and the Remaining Shareholders Agreement(s) is RMB717.3 million, which shall be satisfied by Huada Electronics in cash. Incidental to the Huada Semiconductor Acquisition, the Company entered into:

- (a) the 2015-2018 Business Services Agreement with CEC, pursuant to which the CEC Group will provide products processing, testing and assembling services to the Group and purchase integrated circuit cards and smart cards modules and chips from the Group and the Group will purchase raw materials, modules, software and equipment from the CEC Group.
- (b) the 2015-2018 Financial Services Agreement with CEC Finance, pursuant to which CEC Finance will provide a range of financial services to the Group.

An Independent Board Committee has been established to advise the Independent Shareholders in respect of the terms of the Shanghai Huahong Acquisition Agreements, the 2015-2018 Business Services Agreement and the 2015-2018 Financial Services Agreement and their respective proposed caps. In this respect, Altus Capital has been appointed as the independent financial adviser to the Independent Board Committee and the Independent Shareholders.

The purpose of this circular is to provide you with, among other things, (i) information on the Shanghai Huahong Acquisition, the 2015-2018 Business Services Agreement and the 2015-2018 Financial Services Agreement and their respective proposed caps; (ii) to set out the advice from Altus Capital, the independent financial adviser to the Independent Board Committee and the Independent Shareholders in respect of the terms of the same; (iii) the recommendation from the Independent Board Committee; (iv) financial information of the Group; (v) financial information of Huahong; (vi) unaudited pro forma financial information of the Enlarged Group; and (vii) to give notice of SGM.

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## LETTER FROM THE BOARD

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### THE ACQUISITION OF A 95.64% EQUITY INTEREST IN HUAHONG

**(1) Huada Semiconductor Agreement**

|                |                                   |
|----------------|-----------------------------------|
| Date:          | 26 June 2015                      |
| Vendor:        | Huada Semiconductor               |
| Purchaser:     | Huada Electronics                 |
| Subject asset: | 73.43% equity interest in Huahong |
| Consideration: | RMB550.7 million                  |

**(2) Individual Vendor Agreement(s)**

|                          |                                                                |
|--------------------------|----------------------------------------------------------------|
| Date:                    | 26 June 2015                                                   |
| Vendors:                 | Individual Vendors <sup>1</sup> (excluding Other Shareholders) |
| Purchaser:               | Huada Electronics                                              |
| Subject asset:           | an aggregate of a 9.95% equity interest in Huahong             |
| Aggregate consideration: | RMB74.6 million                                                |

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<sup>1.</sup> Each of the Individual Vendors (excluding Other Shareholders) will enter into separate Individual Vendor Agreement with Huada Electronics for the sale of his/her respective equity interest in Huahong.

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## LETTER FROM THE BOARD

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### (3) Supplemental Huahong Group Agreement

Further to the Huahong Group Agreement, Huada Electronics and Huahong Group entered into the Supplemental Huahong Group Agreement to further determine certain terms under the Huahong Group Acquisition including, among other things, the amount of consideration, conditions precedent and the terms of completion.

|                |                                  |
|----------------|----------------------------------|
| Date:          | 27 August 2015                   |
| Vendor:        | Huahong Group                    |
| Purchaser:     | Huada Electronics                |
| Subject asset: | 7.62% equity interest in Huahong |
| Consideration: | RMB57.1 million                  |

### (4) Remaining Shareholders Agreement(s)

|                          |                                                                |
|--------------------------|----------------------------------------------------------------|
| Date:                    | 27 August 2015                                                 |
| Vendors:                 | Individual Vendors <sup>1</sup> (excluding Other Shareholders) |
| Purchaser:               | Huada Electronics                                              |
| Subject asset:           | an aggregate of a 4.64% equity interest in Huahong             |
| Aggregate consideration: | RMB34.9 million                                                |

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<sup>1</sup>. Each of the Individual Vendors (excluding Other Shareholders) will enter into separate Remaining Shareholders Agreement with Huada Electronics for the sale of his/her respective equity interest in Huahong

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## LETTER FROM THE BOARD

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### Consideration

The total aggregate consideration for the Shanghai Huahong Acquisition of RMB717.3 million represents a price to 2014<sup>1</sup> earnings multiples of 13.4 and a price to 2014<sup>1</sup> sales multiples of 1.6 of Huahong, and was determined after arm's length negotiations between the parties to the Shanghai Huahong Acquisition Agreements having regard to the following:

- (i) the price to earnings multiples and the price to sales multiples of companies<sup>2</sup> listed on the Stock Exchange which are engaged in similar businesses as Huahong as an indicative range to determine the consideration, taking into account the discount to valuation given that Huahong is an unlisted company;
- (ii) the historical financial performance of Huahong;
- (iii) the business prospect of Huahong; and
- (iv) the potential benefits to the Group after Completion.

The consideration payable under the Supplemental Huahong Group Agreement shall be paid in the following manner:

- (i) Huada Electronics shall transfer the consideration into the nominated account of SUAEE;
- (ii) SUAEE shall complete all procedures required for such equity transfer; and
- (iii) on the date agreed between Huahong Group and Huada Electronics (which shall not be later than the period allowed under the requirements of the state-owned asset administrative management and SUAEE), SUAEE shall transfer the consideration into the bank account nominated by Huahong Group after the completion of the procedures set out in paragraph (ii) above.

The date of the Certificate of Assets and Equity Exchange issued by SUAEE shall be the date of completion of the Huahong Group Acquisition.

The consideration payable under the Huada Semiconductor Agreement, the Individual Agreement(s) and the Remaining Shareholders Agreement(s) shall be paid within five business days from the date of Completion.

# LETTER FROM THE BOARD

1. Based on the audited financial results of Huahong for the year ended 31 December 2014.

| Company name<br>(stock code)                                       | Principal business                                                                                                             | Market<br>capitalisation<br>as at<br>26 June 2015<br><i>HK\$ (million)</i> | Revenue<br>(Note 1)<br><i>HK\$ (million)</i> | Price to sales<br>ratio<br>("P/S Ratio")<br>(Note 2)<br>(times) | Price to<br>earnings<br>ratio<br>("P/E Ratio")<br>(Note 3)<br>(times) |
|--------------------------------------------------------------------|--------------------------------------------------------------------------------------------------------------------------------|----------------------------------------------------------------------------|----------------------------------------------|-----------------------------------------------------------------|-----------------------------------------------------------------------|
| Advanced Semiconductor Manufacturing Corporation Limited<br>(3355) | Manufacturing and sale of<br>semiconductors                                                                                    | 1,187.9                                                                    | 1,004.2                                      | 1.2                                                             | 19.4                                                                  |
| China Electronics Corporation Holdings Company Limited<br>(0085)   | Design and sale of integrated circuit<br>chips, develop and manage of<br>electronic information technology<br>industrial parks | 8,687.9                                                                    | 1,357.1                                      | 6.4                                                             | 51.1                                                                  |
| Semiconductor Manufacturing International Corporation<br>(0981)    | Manufacturing of semiconductors                                                                                                | 35,860.0                                                                   | 15,267.2                                     | 2.3                                                             | 30.2                                                                  |
| Shanghai Fudan Microelectronics Group Company Limited<br>(1385)    | Design and sale of integrated circuit<br>products                                                                              | 3,318.8                                                                    | 1,062.8                                      | 3.1                                                             | 15.7                                                                  |
| Sino-Tech International Holdings Limited (0724)                    | Manufacturing and trading of<br>electronic parts and components                                                                | 1,487.8                                                                    | 599.9                                        | 2.5                                                             | –<br>(Note 4)                                                         |
| Solomon Systech (International) Limited (2878)                     | Design, develop and sale of<br>integrated circuit products                                                                     | 1,307.8                                                                    | 465.6                                        | 2.8                                                             | –<br>(Note 4)                                                         |
|                                                                    |                                                                                                                                |                                                                            | <b>Minimum:</b>                              | 1.2                                                             | 15.7                                                                  |
|                                                                    |                                                                                                                                |                                                                            | <b>Maximum:</b>                              | 6.4                                                             | 51.1                                                                  |
| Huahong (Note 5)                                                   |                                                                                                                                |                                                                            |                                              | 1.6                                                             | 13.4                                                                  |

Source: Respective annual reports of the companies and the website of the Stock Exchange.

Notes:

- Based on the latest published audited figures for the year ended 31 December 2014.
- The P/S Ratios of the companies are derived from dividing the market capitalisation as at 26 June 2015 by the latest published audited revenue of the respective group.
- The P/E Ratios of the companies are derived from dividing the market capitalisation as at 26 June 2015 by the latest published audited profit attributable to owners of the respective companies.
- No P/E Ratio is presented as the relevant group recorded a loss.
- The P/S Ratio and P/E Ratio are calculated based on the total aggregate consideration for the Shanghai Huahong Acquisition.

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## LETTER FROM THE BOARD

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The Company expects that the consideration will be satisfied in cash from internal resources and borrowing facilities of the Group, if needed.

### Conditions precedents

The Shanghai Huahong Acquisition Agreements shall not proceed to Completion unless the following conditions precedents have been satisfied or have been waived by Huada Electronics:

- (i) the Company having obtained approval from the Independent Shareholders pursuant to the Listing Rules in respect of the transactions contemplated by the Shanghai Huahong Acquisition Agreements and any continuing connected transactions (as defined in the Listing Rules) arising thereof;
- (ii) the Huada Semiconductor Agreement, the Individual Vendor Agreement(s), the Supplemental Huahong Group Agreement and the Remaining Shareholders Agreement(s) having been duly signed by both parties thereto, respectively;
- (iii) Huada Semiconductor or Huahong Group (as the case may be) and Huada Electronics having completed its internal approval procedures for the transfer of such equity interest and having obtained written internal approvals in relation thereto;
- (iv) the equity transfer having been approved at a shareholders' meeting by more than half of the shareholders of Huahong (excluding Huada Semiconductor under the Huada Semiconductor Agreement, each of the Individual Vendors under the relevant Individual Vendor Agreement(s) or the relevant Remaining Shareholders Agreement(s), and Huahong Group under the Supplemental Huahong Group Agreement (as the case may be), respectively);
- (v) subject to the exercise of pre-emption rights by the other shareholders of Huahong who are not parties to the Shanghai Huahong Acquisition Agreements, and/or such shareholders who have elected not to transfer all, or part of, their equity interests in Huahong, Huada Electronics having the ability to acquire not less than 50% of the equity interest in Huahong;
- (vi) such equity transfer under the Shanghai Huahong Acquisition Agreements having been approved by the relevant department for the supervision and administration of state-owned assets and the filings for the evaluation of state-owned assets having been completed;

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## LETTER FROM THE BOARD

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- (vii) all other necessary pre-examinations, pre-approvals or filing procedures having been completed in connection with the Shanghai Huahong Acquisition Agreements in the PRC;
- (viii) the equity transfer having been registered with the relevant administration for industry and commerce, and a new business license having been obtained;
- (ix) all statements, representations and warranties being true, accurate and not misleading in any respect at the time of Completion; and
- (x) details of the bank account to which the consideration for the Shanghai Huahong Acquisition shall be paid into having been provided to Huada Electronics.

### Completion

Completion shall take place on the fifth business day after the above conditions precedents have been satisfied (or waived by Huada Electronics) and the relevant part(ies) shall ensure:

- (i) the delivery of relevant documents to Huada Electronics confirming that the conditions precedents under the Shanghai Huahong Acquisition Agreements have been satisfied (or waived by Huada Electronics);
- (ii) that Huahong submits a certificate signed by its legal representative on the date of Completion confirming that the conditions precedents under the Shanghai Huahong Acquisition Agreements have been satisfied (or waived by Huada Electronics), and that no material adverse change has occurred as at the date of Completion;
- (iii) that a capital contribution certificate (in the form as prescribed under the PRC laws) signed by the legal representative of Huahong with its company seal affixed thereto be issued to Huada Electronics, stating that Huada Electronics owns the equity interest in Huahong as stipulated under each of the Shanghai Huahong Acquisition Agreements, with an aggregate of a 95.64% equity interest in Huahong (subject to the exercise of pre-emption rights by relevant shareholders of Huahong under each of the Shanghai Huahong Acquisition Agreements (as the case may be), respectively); and
- (iv) that Huada Electronics be entered in the register of members of Huahong as the legal and beneficial owner of an aggregate of a 95.64% equity interest in Huahong, and that a copy of the revised register of members be provided to Huada Electronics.

Upon completion of the Shanghai Huahong Acquisition, Huahong will become a subsidiary of the Company and the assets, liabilities and financial results of Huahong will be consolidated into the consolidated financial statements of the Company.

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## LETTER FROM THE BOARD

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### INFORMATION ON HUAHONG

#### Overview

Established in 1998 under the laws of the PRC, Huahong is an industrial leader in the design of the integrated circuit sector in the PRC. It has a comprehensive domestic smart card product line, with technology focusing on the design and system development of contact, contactless and dual-interface integrated circuit chips, which are widely used in sectors such as social security (social security cards), telecommunications (SIM cards), public transport (public transport cards), identity authentication (identity cards and residence permits), electronic travel documents (electronic passports) and financial security (bank cards). Huahong also focuses on providing customers with system solutions to address their business and operational challenges. In recent years, Huahong launched a series of solutions including the public transport one-card pass solution, residence permit solution, Shanghai World Expo ticketing solution, commercial encryption access control system solution, and multi-applications financial solution. These solutions embrace the technical elements of application software, key management system and encrypted integrated circuit chips to form the application-oriented and customer-oriented solutions that enhance the efficiency and security of supply chains, transactions and the authentication of goods and people.

Huahong emphasises original innovation and integrated innovation capabilities, and attaches great importance to scientific discovery and technology invention. Over the years, Huahong has obtained 165 patents, 55 registered integrated circuit layout designs and 21 computer software copyrights through its independent innovation development strategy.

In November 2013, one of the dual-interface integrated circuit chips for security control independently researched and developed by Huahong, was accredited with the Common Criteria Evaluation Assurance Level 4+ Certificate (an international standard for security certification). In the following year, Huahong was also accredited with the EMVCo certificate (security certification). Huahong became the only integrated circuit chip design company in the PRC which was accredited with both certifications. In addition, such dual-interface integrated circuit chip was certified by the State Cryptography Administration Office of Security Commercial Code, PRC, and was accredited with the full qualification certificate by UnionPay, a bank card association established under the approval of the State Council of the PRC and the PBOC. Huahong is the sole PRC supplier of bank cards (at state secret level) for the Industrial and Commercial Bank of China Limited and one of the PRC suppliers of bank cards (at state secret level) for the China Construction Bank Corporation. Huahong is now well positioned to tap into the domestic market where over 90% of the integrated circuit chips for bank cards are imported from overseas.

Mr. Dong Haoran, Mr. Wang Liqiang, Mr. Ma Yuchuan, Mr. Xiang Xiang and Mr. Li Rongxin are currently directors of Huahong. Mr. Dong Haoran is a director of the Company, a director and the general manager of Huada Semiconductor and a director of China Huada.

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## LETTER FROM THE BOARD

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### Financial information on Huahong

Huahong's revenue was mainly derived from the sale of integrated circuit products. For further discussion on the revenue, costs and assets of Huahong, please refer to "Appendix I – Management Discussion and Analysis of Huahong".

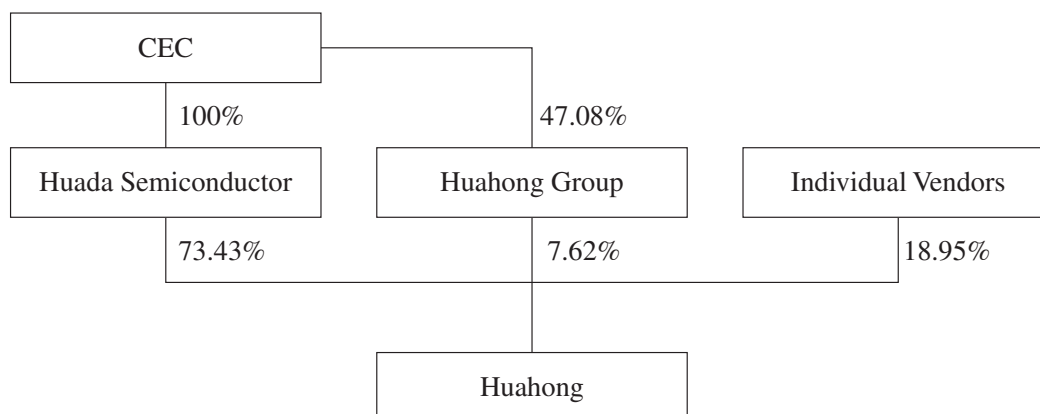
Based on the accountant's report of Huahong prepared in accordance with the Hong Kong Financial Reporting Standards as set out in Appendix III to this circular, the audited consolidated net assets of Huahong was RMB341.7 million as at 30 April 2015. The following table shows the audited consolidated results of Huahong for each of the years ended 31 December 2012, 2013 and 2014 and the four months ended 30 April 2015 as extracted from the accountant's report of Huahong as set out in Appendix III to this circular:

|                                   | Year ended 31 December |           |           | Four months ended |
|-----------------------------------|------------------------|-----------|-----------|-------------------|
|                                   | 2012                   | 2013      | 2014      | 30 April          |
|                                   | (RMB'000)              | (RMB'000) | (RMB'000) | 2015              |
|                                   |                        |           |           | (RMB'000)         |
| Profit/(loss) before taxation     | 40,430                 | 64,238    | 51,800    | (2,261)           |
| Profit/(loss) for the year/period | 35,085                 | 64,238    | 56,069    | (2,261)           |

The Company understands that the total investment cost for Huahong by Huada Semiconductor, Huahong Group and the Individual Vendors (excluding Other Shareholders) was RMB260.8 million, RMB51.3 million and RMB23.1 million, respectively.

### Shareholding structure of Huahong

The following is the simplified shareholding structure chart of Huahong prior to Completion:

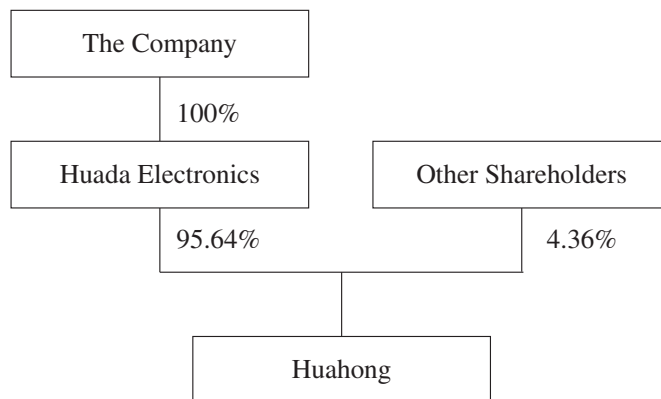


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## LETTER FROM THE BOARD

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The following is the simplified shareholding structure chart of Huahong immediately after Completion:



### **Financial effects of the Shanghai Huahong Acquisition**

The Group has applied principles of merger accounting as prescribed in Hong Kong Accounting Guideline 5 “Merger Accounting for Common Control Combinations” issued by the Hong Kong Institute of Certified Public Accountants for the Shanghai Huahong Acquisition. Under merger accounting, the consolidated financial statements incorporates the financial statements of the combining entities or businesses in which the common control combination occurs as if they had been combined from the date when the combining entities or businesses first came under the control of the controlling party.

The net assets of the combining entities or businesses are combined using the existing book values from the controlling parties’ perspective. No amount is recognised in consideration for goodwill or excess of acquirers’ interest in the net fair value of acquiree’s identifiable assets, liabilities and contingent liabilities over cost at the time of common control combination. Set out in Appendix IV to this circular is the “Unaudited Pro Forma Financial Information of the Enlarged Group” and the basis of preparation thereon.

### ***Assets and liabilities***

Upon Completion, Huada Electronics will directly hold a 95.64% equity interest in Huahong, which will become a subsidiary of the Company. The assets and liabilities of Huahong will be consolidated into the consolidated financial statements of the Company.

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## LETTER FROM THE BOARD

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### ***Earnings***

The results of Huahong will be consolidated into the consolidated financial statements of the Company upon Completion.

### ***Working capital***

Taking into account the financial resources available to the Enlarged Group, including the internally generated funds and the available committed borrowing facilities, the Directors are of the opinion that in the absence of unforeseeable circumstances, the Enlarged Group has sufficient working capital available for its requirements, that is for at least the next 12 months from the date of this circular.

### ***Indebtedness***

As at 31 August 2015, being the latest practicable date for the purpose of this indebtedness statement prior to the date of this circular, the Group and Huahong had outstanding borrowings of HK\$4,516.6 million and HK\$18.2 million, respectively.

The analysis of the borrowings of the Group as at 31 August 2015 is as follows:

|                               | <b>As at<br/>31 August<br/>2015<br/>(HK\$ million)</b> |
|-------------------------------|--------------------------------------------------------|
| Current bank borrowings       | 1,213.1                                                |
| Unsecured corporate bonds (a) | <u>3,303.5</u>                                         |
|                               | <u><u>4,516.6</u></u>                                  |

- (a) As at 31 August 2015, the Group had outstanding unsecured bonds due 2017 in the principal amount of RMB2,750.0 million, the bonds will mature on 16 January 2017 and are listed on the Stock Exchange. The carrying amount of the unsecured bonds is HK\$3,303.5 million as at 31 August 2015.

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## LETTER FROM THE BOARD

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The analysis of the borrowings of Huahong as at 31 August 2015 is as follows:

**As at**  
**31 August**  
**2015**  
*(HK\$ million)*

|                                     |             |
|-------------------------------------|-------------|
| Current borrowings from CEC Finance | <u>18.2</u> |
|-------------------------------------|-------------|

Save as disclosed above and apart from intra-group liabilities and normal trade payables, the Enlarged Group did not have, as at 31 August 2015, any mortgages, charges, debentures, debt securities issued and outstanding, and authorised or otherwise created but unissued, outstanding borrowings or indebtedness in the nature of borrowings including term loans, bank overdrafts, liabilities under acceptances, acceptance credits, hire purchase and finance lease commitments or other similar indebtedness, or any guarantees or other material contingent liabilities.

### ***Gearing ratios***

As at 31 December 2014, the gearing ratio of the Group was 83.6% (calculated as the total liabilities over total assets of the Group). As set out in Appendix IV to this circular, assuming 30 June 2015 is the date of Completion, the gearing ratio of the Group will be 89.3%.

As at 31 December 2014, the gearing ratio of the Group was 79.4% (calculated as the total net debt over total capital of the Group). As set out in Appendix IV to this circular, assuming 30 June 2015 is the date of Completion, the gearing ratio of the Group will be 84.5%.

### **CONTINUING CONNECTED TRANSACTIONS – 2015-2018 BUSINESS SERVICES AGREEMENT WITH CEC**

#### **Background**

The Company refers to its announcement dated 7 May 2013 and the circular dated 28 May 2013 in relation to certain continuing connected transactions between the Group and the CEC Group contemplated under the 2013-2016 Business Services Agreement. The 2013-2016 Business Services Agreement will expire on 30 June 2016. Huahong has on-going transactions with the CEC Group which are similar to those contemplated under the 2013-2016 Business Services Agreement in its ordinary and usual course of business. These transactions will, after the completion of the Huada Semiconductor Acquisition, become continuing connected transactions of the Company.

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## LETTER FROM THE BOARD

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On 26 June 2015, in order to streamline the existing continuing connected transactions contemplated under the 2013-2016 Business Services Agreement, and to facilitate the Group's production and operation after the completion of the Huada Semiconductor Acquisition, the Company entered into the 2015-2018 Business Services Agreement with CEC to reflect the terms of the proposed continuing connected transactions and the caps of the transactions thereunder for the period commencing from the completion of the Huada Semiconductor Acquisition until 31 December 2015, each of the years ending 31 December 2016 and 2017 and the six months ending 30 June 2018.

### **2015-2018 Business Services Agreement**

Date: 26 June 2015

Parties: (i) the Company

(ii) CEC

The 2015-2018 Business Services Agreement covers (i) the provision of products processing, testing and assembling services by the CEC Group, and the purchase of raw materials, modules, software and equipment from the CEC Group; and (ii) the sale of integrated circuit cards and smart cards modules and chips to the CEC Group (collectively, the "Business Services"). The 2015-2018 Business Services Agreement provides a framework between the Company and CEC under which the Group and any member of the CEC Group may enter into separate supplemental agreement(s) setting out the terms and conditions for Business Services required from time to time. The 2015-2018 Business Services Agreement was entered into on a non-exclusive basis and does not create any obligations on the Group to enter into any agreement(s) with any member of the CEC Group for Business Services. Any member of the CEC Group is one of a number of companies which the Group may enter into agreement(s) for Business Services. The Group may enter into agreement(s) for Business Services with any member of the CEC Group and/or any other companies, as it sees fit.

Details of the continuing connected transactions contemplated under the 2015-2018 Business Services Agreement are as follows:

- (i) ***Provision of products processing, testing and assembling services by the CEC Group, and the purchase of raw materials, modules, software and equipment from the CEC Group***

The CEC Group will provide products processing, testing and assembling services to the Group for the production of products including integrated circuit cards, smart cards and chips.

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## LETTER FROM THE BOARD

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The Group will also purchase raw materials, modules, software and equipment for the research and development of integrated circuit cards, smart cards and chips from the CEC Group.

***(ii) Sale of products to the CEC Group***

The Group will also sell products including integrated circuit cards and smart cards modules and chips to the CEC Group.

The prices payable and receivable by the Group under the 2015-2018 Business Services Agreement will be determined after arm's length negotiations between the parties with reference to market prices. The prices offered by or to the CEC Group will be no less favourable than "market prices" as defined under the 2015-2018 Business Services Agreement: (a) the prices of similar or comparable type of products or services in similar quantities offered by or to independent third parties in the same geographical area in the ordinary and usual course of business, or, in the absence of which, (b) the prices of similar or comparable type of products or services offered by or to independent third parties in the ordinary and usual course of business.

To ensure that the transactions under the 2015-2018 Business Services Agreement are conducted on normal commercial terms, or on terms no less favorable than terms available to independent third parties, the Group has adopted the following procedures to determine the prices and terms of the transactions. Before confirming the pricing of provision of products processing, testing and assembling services by the CEC Group, and purchase of raw materials, modules, software and equipment from the CEC Group, the Group would refer to two other contemporaneous transactions with independent third parties in similar quantities to determine if the prices and terms offered by the CEC Group are fair, reasonable and no less favorable than those offered by independent third parties, or the pricing of the end products according to the customers order, the complexity of the particular work and the raw materials and technology involved. Before confirming the pricing of sale of products to the CEC Group, the Group would refer to previous transactions with independent third parties in respect of similar products and similar quantities within 6 months and any market information based on the experience of the Group's management, the dealings with other players in the market, and industry level profit margin, which may be available at that time, and make an assessment of the general market price of that type of product.

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## LETTER FROM THE BOARD

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The pricing of the transactions under the 2015-2018 Business Services Agreement are subject to an internal approval process. An application for the approval of a potential transaction is made by the purchasing or sales department (as the case may be) and presented to the legal department and finance department for approval. The legal department and finance department will consider an application from an internal control perspective to ensure that the pricing for such potential transaction are in compliance with the pricing policies as set out in the 2015-2018 Business Services Agreement. Transactions exceeding RMB5 million will be further submitted to any one director of the relevant member of the Group for final approval.

Independent non-executive Directors will conduct an annual review of the transactions (including the pricing mechanism, methods and procedures established by the Company) under the 2015-2018 Business Services Agreement and submit their views to the Board.

Given the above, the Directors consider that there are appropriate internal controls and procedures in place to ensure that the transactions under the 2015-2018 Business Services Agreement will be conducted on normal commercial terms and are not prejudicial to the interests of the Company and the Shareholders as a whole.

The consideration payable and receivable by the Group under the 2015-2018 Business Services Agreement will be settled in cash according to the terms upon which the services or products are provided. Based on historical transactions with the CEC Group, the Company expects that for (i) the majority of the provision of products processing, testing and assembling services by the CEC Group, and (ii) the majority of the purchase of raw materials, modules, software and equipment from the CEC Group, the CEC Group will grant credit terms of between 30 days to 90 days. The Company also expects that the majority of the Group's sale of products to the CEC Group will be given credit terms of between 60 days to 120 days.

The prices payable to or receivable by the Group under each of the separate supplemental agreement(s) are based on the terms under the 2015-2018 Business Services Agreement and are subject to negotiations between the parties, having regard to the Group's internal approval process and the definition of "market prices".

Subject to the approval of the Independent Shareholders, the 2015-2018 Business Services Agreement will take effect from the date of the completion of the Huada Semiconductor Acquisition and will be valid until 30 June 2018. The agreement may be renewed for further terms of three years after its expiration if the parties so agree, subject to compliance with the requirements under the Listing Rules.

The 2015-2018 Business Services Agreement will, upon taking effect, supersede the 2013-2016 Business Services Agreement.

## LETTER FROM THE BOARD

**Historical transaction amounts for each of the years ended 31 December 2012, 2013, 2014 and the four months ended 30 April 2015**

| Type of transaction                                                                                                        | Existing caps<br>for the year<br>ending<br>31 December<br>2015<br>(RMB'000)<br>(Note 1) | Historical transaction amounts for |                   |                   |                                                        |
|----------------------------------------------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------|------------------------------------|-------------------|-------------------|--------------------------------------------------------|
|                                                                                                                            |                                                                                         | the year ended 31 December         |                   |                   | the four<br>months ended<br>30 April 2015<br>(RMB'000) |
|                                                                                                                            |                                                                                         | 2012<br>(RMB'000)                  | 2013<br>(RMB'000) | 2014<br>(RMB'000) |                                                        |
| <b>Products processing, testing and assembling services and purchase of raw materials, modules, software and equipment</b> |                                                                                         |                                    |                   |                   |                                                        |
| – Consideration payable by the Group under the 2013-2016 Business Services Agreement                                       | 1,064,000                                                                               | 475,977                            | 360,445           | 373,949           | 98,094                                                 |
| – <i>Utilisation percentage</i>                                                                                            |                                                                                         | 61.8%                              | 54.9%             | 43.9%             |                                                        |
| – <i>Percentage of cost of sales</i>                                                                                       |                                                                                         | 83.1%                              | 62.0%             | 61.0%             |                                                        |
| – Consideration payable by Huahong (Note 2)                                                                                | –                                                                                       | 41,939                             | 29,728            | 86,501            | 8,569                                                  |
|                                                                                                                            | <u>1,064,000</u>                                                                        | <u>517,916</u>                     | <u>390,173</u>    | <u>460,450</u>    | <u>106,663</u>                                         |
| <b>Sale of products</b>                                                                                                    |                                                                                         |                                    |                   |                   |                                                        |
| – Consideration receivable by the Group under the 2013-2016 Business Services Agreement                                    | 188,000                                                                                 | 82,258                             | 74,170            | 136,730           | 46,600                                                 |
| – <i>Utilisation percentage</i>                                                                                            |                                                                                         | 77.6%                              | 63.9%             | 91.2%             |                                                        |
| – <i>Percentage of revenue</i>                                                                                             |                                                                                         | 8.7%                               | 7.0%              | 12.7%             |                                                        |
| – Consideration receivable by Huahong (Note 2)                                                                             | –                                                                                       | 51,730                             | 34,083            | 35,452            | 7,078                                                  |
|                                                                                                                            | <u>188,000</u>                                                                          | <u>133,988</u>                     | <u>108,253</u>    | <u>172,182</u>    | <u>53,678</u>                                          |

*Notes:*

- The Company confirmed that the consideration payable and receivable by the Group under the 2013-2016 Business Services Agreement for the period commencing from 1 January 2015 until the Latest Practicable Date have not exceeded the caps for the year ending 31 December 2015 set out in the above table.
- Huahong's historical transaction amounts are set out here for illustration as one of the bases for determining the proposed caps under the 2015-2018 Business Services Agreement.

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## LETTER FROM THE BOARD

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### Proposed caps for the 2015-2018 Business Services Agreement

It is expected that for the period commencing from the completion of the Huada Semiconductor Acquisition until 31 December 2015, each of the years ending 31 December 2016 and 2017 and the six months ending 30 June 2018, the consideration payable by the Group to the CEC Group and the consideration receivable by the Group from the CEC Group will not exceed the following respective amounts and such amounts have been set as the proposed caps for the relevant continuing connected transactions contemplated under the 2015-2018 Business Services Agreement accordingly:

| Type of transaction                                                                                                        | For the period<br>commencing<br>from the<br>completion of<br>the Huada<br>Semiconductor<br>Acquisition until | For the year ending 31 December |                   | For the<br>six months<br>ending |
|----------------------------------------------------------------------------------------------------------------------------|--------------------------------------------------------------------------------------------------------------|---------------------------------|-------------------|---------------------------------|
|                                                                                                                            | 31 December 2015<br>(RMB'000)<br>(Note 1)                                                                    | 2016<br>(RMB'000)               | 2017<br>(RMB'000) | 30 June 2018<br>(RMB'000)       |
| <b>Products processing, testing and assembling services and purchase of raw materials, modules, software and equipment</b> |                                                                                                              |                                 |                   |                                 |
| – Consideration payable by the Group                                                                                       | 300,000                                                                                                      | 780,000                         | 1,000,000         | 650,000                         |
| <b>Sale of products</b>                                                                                                    |                                                                                                              |                                 |                   |                                 |
| – Consideration receivable by the Group                                                                                    | 110,000                                                                                                      | 290,000                         | 370,000           | 240,000                         |

*Note:*

- The 2013-2016 Business Services Agreement will expire on 30 June 2016. The 2015-2018 Business Services Agreement will, upon taking effect, supersede the 2013-2016 Business Services Agreement. The 2015-2018 Business Services Agreement is subject to the approval of the Independent Shareholders at the SGM, which is expected to take place after June 2015. As such, the term of the 2015-2018 Business Services Agreement will not exceed three years.

In arriving at the above caps for the consideration payable by the Group for the provision of products processing, testing and assembling services by the CEC Group, and the purchase of raw materials, modules, software and equipment from the CEC Group, the Company has referred to the historical service fees paid by the Group and the historical purchase of raw materials, modules, software and equipment from the CEC Group and has taken into account the expected demand of the products of the Group, the production plan of the Group and the costs of such services,

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## LETTER FROM THE BOARD

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raw materials, modules, software and equipment. The Group's integrated circuits design business comprises the design of integrated circuit chips and the development of application systems. Products processing, testing and assembling services and purchase of raw materials, modules, software and equipment are usually conducted outside the Group, and are regarded as different steps in the production process in the Group's business model. As such, the Company considers it appropriate to group the transaction amounts under the same proposed caps. A significant portion of the historical transaction amounts and the proposed caps, is derived from, and based on products processing and assembling services.

In arriving at the above caps for the consideration receivable by the Group for the sale of products to the CEC Group, the Company has referred to the historical sales, the expected demand of the Group's products by the CEC Group and the order status of the products.

The respective proposed caps for (i) the provision of products processing, testing and assembling services by the CEC Group and the purchase of raw materials, modules, software and equipment from the CEC Group, and (ii) the sale of products to the CEC Group for the period commencing from the completion of the Huada Semiconductor Acquisition until 31 December 2015 were based on an assumed increase of approximately 30% from the respective historical transaction amounts for the year ended 31 December 2014 and the purchase orders already received by the Group during the first half of 2015. The proposed caps for the years ending 31 December 2016 and 2017 and the six months ending 30 June 2018 were based on an increase of approximately 30%, 28% and 30% from the proposed caps for the previous year. The proposed caps are based on the historical pricing of comparable products, assuming no changes in prices.

The Company is aware of the potential growth of the PRC smart cards industry. According to the 2015-2020 Market Analysis and Strategic Consultancy Report in respect of the Integrated Circuit Chip Bank Cards of China (《2015-2020年中國銀行IC卡市場分析預測及戰略諮詢報告》) and Analysis of Issued Volume and Market Penetration of Integrated Circuit Chip Bank Cards of China in 2014 (《2014年中國金融IC卡行業發卡量及參透率分析》) issued by Beijing Zhiyan Kexin Consulting Co., Ltd (北京智研科信諮詢有限公司)<sup>1</sup> in March and August 2015, respectively and published on China Industry Information website, based on the requirements of the PBOC, the issue and use of magnetic stripe bank cards will cease gradually in the PRC from 2015 and will be replaced by integrated circuit chip bank cards. This replacement process had commenced gradually in various regions, and it is expected in the industry that the number of integrated circuit chip bank cards which will be issued in the PRC annually may reach hundreds of millions in the coming years. The global market capacity of SIM cards is also growing steadily, and there are new market opportunities created by the development of the mobile payment and Internet of Things sectors. According to statistics published by the China Semiconductor Industry Association<sup>2</sup>, the total

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<sup>1</sup> Established in 2008, Beijing Zhiyan Kexin Consulting Co., Ltd is principally engaged in corporate management consultancy and business information consultancy businesses. Currently, it operates and maintains various industrial research websites and consultancy service platforms, provides professional information and data to third parties, such as industry research reports, market surveys and statistical data, etc.

<sup>2</sup> The China Semiconductor Industry Association is an industrial and national non-profit making organization which was established in 1990 by the institutions, experts and other relevant enterprises in the PRC semiconductor sector engaged in the production, design, scientific research, development, operation, application, and education of integrated circuits, discrete semiconductor devices, semiconductor materials and equipment.

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## LETTER FROM THE BOARD

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revenue generated by the integrated circuit industry in PRC for the year ended 31 December 2014 increased 20.2% to RMB301,540 million as compared to the year ended 31 December 2013. The total revenue generated from the design of integrated circuits, one of the key stages in the supply chain, increased 29.5% to RMB104,740 million for the year ended 31 December 2014 as compared to the year ended 31 December 2013. The Company therefore considers that the increase in the proposed caps of approximately 30% per annum from the year ending 31 December 2015 onwards is in line with industry trends.

### **CONTINUING CONNECTED TRANSACTIONS – 2015-2018 FINANCIAL SERVICES AGREEMENT WITH CEC FINANCE**

#### **Background**

The Company refers to its announcements dated 7 May 2013 and 7 July 2013 and the circulars dated 28 May 2013 and 28 August 2013 in relation to certain continuing connected transactions between the Group and CEC Finance contemplated under the 2013-2016 Financial Services Agreement and the CEC Technology Financial Services Agreement, respectively (together, the “2013 Financial Services Agreements”). The 2013 Financial Services Agreements will expire on 30 June 2016. Huahong has on-going transactions with CEC Finance which are similar to those contemplated under the 2013 Financial Services Agreements in its ordinary and usual course of business. These transactions will, after the completion of the Huada Semiconductor Acquisition, become continuing connected transactions of the Company.

On 26 June 2015, in order to streamline the existing continuing connected transactions contemplated under the 2013 Financial Services Agreements and to facilitate the Group’s operation after the completion of the Huada Semiconductor Acquisition, the Company entered into the 2015-2018 Financial Services Agreement with CEC Finance to reflect the terms of the proposed continuing connected transactions and the caps of the transactions thereunder for the period commencing from the completion of the Huada Semiconductor Acquisition until 31 December 2015, each of the years ending 31 December 2016 and 2017 and the six months ending 30 June 2018.

#### **2015-2018 Financial Services Agreement**

|          |                  |
|----------|------------------|
| Date:    | 26 June 2015     |
| Parties: | (i) the Company  |
|          | (ii) CEC Finance |

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## LETTER FROM THE BOARD

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Pursuant to the 2015-2018 Financial Services Agreement, CEC Finance will provide a range of financial services to the Group and the Group will utilise such financial services on a non-exclusive basis. The financial services to be provided by CEC Finance to the Group under the 2015-2018 Financial Services Agreement include:

- (a) deposit services, including but not limited to, time deposits, call deposits and negotiable deposits;
- (b) provision of financial assistance, including but not limited to, unsecured RMB and foreign currencies loans, finance leasing, discounting of bank acceptance bills and commercial acceptance bills and factoring of account receivables; and
- (c) provision of fee-based and commission-based financial services, including but not limited to, guarantee services, fund management, agency services and financial consultancy services.

The 2015-2018 Financial Services Agreement provides a framework between the Company and CEC Finance under which any member of the Group and CEC Finance may enter into separate supplemental agreement(s) setting out the terms and conditions for various financial services required from time to time. The interest rates offered by CEC Finance under the 2015-2018 Financial Services Agreement are subject to negotiations between the parties.

The 2015-2018 Financial Services Agreement was entered into on a non-exclusive basis and does not create any obligations on the part of the Group to utilise any particular services of CEC Finance. Other than time deposits which have specified deposit terms, the Group may at any time withdraw the funds deposited with CEC Finance without incurring any penalty.

The interest rates for the Group's deposits with CEC Finance will be determined by reference to, and shall not be less than, the rates offered to the Group by other domestic commercial banks for comparable deposits.

The interest rates for the financial assistance provided by CEC Finance to the Group will be determined by reference to, and shall not be higher than, the rates offered to the Group by other domestic commercial banks for comparable financial assistance.

The fees and commissions for the fee-based and commission-based financial services provided by CEC Finance to the Group will be determined by reference to, and shall not be higher than, the fees and commissions charged by other domestic commercial banks or financial institutions for the same type of financial services.

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## LETTER FROM THE BOARD

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To ensure that the transactions under the 2015-2018 Financial Services Agreement are conducted on normal commercial terms, or on terms no less favorable than terms available to independent third parties, the Group has adopted the following procedures to determine the price and terms of the transactions. Before making a deposit with, seeking financial assistance from or using fee-based and commission-based financial services from CEC Finance, the Group would obtain the interest rates and/or fees/commissions (as appropriate) offered by one or two reputable domestic commercial banks or financial institutions which the Group has established business relationship and compare that with the interest rates and/or fees/commissions offered by CEC Finance. CEC Finance is one of a number of financial institutions which provide financial services to the Group. The Group may obtain financial services available from CEC Finance, and/or any other financial institutions, as it sees fit.

The interest rates offered by CEC Finance under the 2015-2018 Financial Services Agreement are subject to an internal approval process. In respect of any deposit services or financial assistance provided by CEC Finance to the Group, an internal application is submitted to the finance departments of the relevant member of the Group procuring such services for approval. For transactions exceeding RMB100 million, the interest rates are subject to further approval by any one Director.

Independent non-executive Directors will conduct an annual review of the transactions (including the rates offered by CEC Finance) under the 2015-2018 Financial Services Agreement and submit their views to the Board.

Given the above, the Directors consider that there are appropriate internal controls and procedures in place to ensure that the transactions under the 2015-2018 Financial Services Agreement will be conducted on normal commercial terms and are not prejudicial to the interests of the Company and the Shareholders as a whole.

The interests on the deposits and the financial assistance, and the fees and commissions for the fee-based and commission-based financial services will be settled in cash according to the terms of the deposits, financial assistance or financial services provided.

Subject to the approval of the Independent Shareholders, the 2015-2018 Financial Services Agreement will take effect from the date of the completion of the Huada Semiconductor Acquisition and will be valid until 30 June 2018. The agreement may be renewed for further terms of three years upon expiration if the parties so agree, subject to compliance with the requirements under the Listing Rules.

The 2015-2018 Financial Services Agreement will, upon taking effect, supersede the 2013 Financial Services Agreements.

## LETTER FROM THE BOARD

**Historical transaction amounts for each of the years ended 31 December 2012, 2013, 2014 and the four months ended 30 April 2015**

| Type of transaction                                                                                                                                         | Existing caps<br>for the year<br>ending<br>31 December<br>2015<br><i>(RMB'000)</i><br><i>(Note 1)</i> | Historical transaction amounts for |                          |                                             |                                                                                  |
|-------------------------------------------------------------------------------------------------------------------------------------------------------------|-------------------------------------------------------------------------------------------------------|------------------------------------|--------------------------|---------------------------------------------|----------------------------------------------------------------------------------|
|                                                                                                                                                             |                                                                                                       | the year ended 31 December         |                          |                                             | the four<br>months ended<br>30 April 2015<br><i>(RMB'000)</i><br><i>(Note 3)</i> |
|                                                                                                                                                             |                                                                                                       | 2012<br><i>(RMB'000)</i>           | 2013<br><i>(RMB'000)</i> | 2014<br><i>(RMB'000)</i><br><i>(Note 3)</i> |                                                                                  |
| <b>Provision of deposit services by CEC Finance</b>                                                                                                         |                                                                                                       |                                    |                          |                                             |                                                                                  |
| Maximum daily balance of deposits<br>(together with the interests accrued<br>thereon) maintained with CEC<br>Finance by:                                    |                                                                                                       |                                    |                          |                                             |                                                                                  |
| – the Group under the 2013<br>Financial Services Agreements                                                                                                 | 480,000                                                                                               | 80,000                             | 276,000                  | 398,351                                     | 383,581                                                                          |
| – Huahong <i>(Note 4)</i>                                                                                                                                   | –                                                                                                     | 410,374                            | 350,385                  | 307,050                                     | 95,229                                                                           |
|                                                                                                                                                             | <u>480,000</u>                                                                                        | <u>490,374</u>                     | <u>626,385</u>           | <u>705,401</u>                              | <u>478,810</u>                                                                   |
| <b>Provision of financial assistance by CEC Finance</b>                                                                                                     |                                                                                                       |                                    |                          |                                             |                                                                                  |
| Maximum daily balance of<br>financial assistance provided by<br>CEC Finance to the Group<br>under the 2013 Financial<br>Services Agreements <i>(Note 2)</i> | 480,000                                                                                               | –                                  | –                        | 361,000                                     | 50,000                                                                           |
|                                                                                                                                                             | <u>480,000</u>                                                                                        | <u>–</u>                           | <u>–</u>                 | <u>361,000</u>                              | <u>50,000</u>                                                                    |
| <b>Provision of fee-based and commission-based financial services by CEC Finance</b>                                                                        |                                                                                                       |                                    |                          |                                             |                                                                                  |
| Fees and commissions payable by:                                                                                                                            |                                                                                                       |                                    |                          |                                             |                                                                                  |
| – the Group under the 2013<br>Financial Services Agreements                                                                                                 | 10,750                                                                                                | –                                  | –                        | 445                                         | 28                                                                               |
| – Huahong <i>(Note 4)</i>                                                                                                                                   | –                                                                                                     | 31                                 | 22                       | 16                                          | –                                                                                |
|                                                                                                                                                             | <u>10,750</u>                                                                                         | <u>31</u>                          | <u>22</u>                | <u>461</u>                                  | <u>28</u>                                                                        |

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## LETTER FROM THE BOARD

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*Notes:*

1. The Company confirmed that the maximum daily balance of the deposits and the financial assistance, and the fees and commissions for the fee-based and commission-based financial services payable by the Group under the 2013 Financial Services Agreements for the period commencing from 1 January 2015 until the Latest Practicable Date have not exceeded the caps for the year ending 31 December 2015 set out in the above table.
2. Apart from unsecured RMB and foreign currencies loans, the Group may be required to provide security for certain types of financial assistance to be provided by CEC Finance.
3. CEC Technology became a wholly-owned subsidiary of the Company following the completion of the acquisition of CEC Technology on 26 June 2014. The transactions between CEC Technology and its subsidiaries and the CEC Group have since then become continuing connected transactions of the Company.
4. Huahong's historical transaction amounts are set out here for illustration as one of the bases for determining the proposed caps under the 2015-2018 Financial Services Agreement.

# LETTER FROM THE BOARD

## Proposed caps for the 2015-2018 Financial Services Agreement

It is expected that for the period commencing from the completion of the Huada Semiconductor Acquisition until 31 December 2015, each of the years ending 31 December 2016 and 2017 and the six months ending 30 June 2018, the maximum daily balance of the deposits and the financial assistance, and the fees and commissions for the fee-based and commission-based financial services payable by the Group, will not exceed the following respective amounts and such amounts have been set as the proposed caps for the relevant continuing connected transactions contemplated under the 2015-2018 Financial Services Agreement accordingly:

| Type of transaction                                                                                                               | For the period<br>commencing from<br>the completion of<br>the Huada<br>Semiconductor<br>Acquisition until | For the year ending 31 December |                   | For the<br>six months<br>ending |
|-----------------------------------------------------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------|---------------------------------|-------------------|---------------------------------|
|                                                                                                                                   | 31 December 2015<br>(RMB'000)<br>(Note 1)                                                                 | 2016<br>(RMB'000)               | 2017<br>(RMB'000) | 30 June 2018<br>(RMB'000)       |
| <b>Provision of deposit services<br/>by CEC Finance</b>                                                                           |                                                                                                           |                                 |                   |                                 |
| Maximum daily balance of deposits<br>(together with the interests accrued<br>thereon) maintained by the Group with<br>CEC Finance | 700,000                                                                                                   | 740,000                         | 780,000           | 820,000                         |
| <b>Provision of financial assistance<br/>by CEC Finance</b>                                                                       |                                                                                                           |                                 |                   |                                 |
| Maximum daily balance of financial<br>assistance provided by CEC Finance to<br>the Group (Note 2)                                 | 700,000                                                                                                   | 740,000                         | 780,000           | 820,000                         |
| <b>Provision of fee-based and<br/>commission-based financial services<br/>by CEC Finance</b>                                      |                                                                                                           |                                 |                   |                                 |
| Fees and commissions payable by the<br>Group to CEC Finance                                                                       | 5,000                                                                                                     | 10,000                          | 10,000            | 5,000                           |

### Notes:

- The 2013 Financial Services Agreements will expire on 30 June 2016. The 2015-2018 Financial Services Agreement will, upon taking effect, supersede the 2013 Financial Services Agreements. The 2015-2018 Financial Services Agreement is subject to the approval of the Independent Shareholders at the SGM, which is expected to take place after June 2015. As such, the term of the 2015-2018 Financial Services Agreement will not exceed three years.
- Apart from unsecured RMB and foreign currencies loans, the Group may be required to provide security for certain types of financial assistance to be provided by CEC Finance.

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## LETTER FROM THE BOARD

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The maximum proposed caps for the 2015-2018 Financial Services Agreement were determined by taking into consideration of the caps relating to the provision of financial assistance by CEC Finance to the Group. In particular, as part of its treasury policy, CEC is prepared to provide financial assistance of the above amounts to the Group through CEC Finance. The proposed caps represent the maximum amount of funds that CEC Finance can provide to the Group and are determined with reference to the estimated capital and operational needs of the Group, which are based on CEC Finance's internal assessment on the maximum amount of unsecured and secured financial assistance which they may provide to the Group. In return for the financial assistance provided by CEC Finance, the proposed maximum daily balance of deposits was set at a level which is the same as the limit of the financial assistance that could be provided.

The above caps for the provision of financial assistance by CEC Finance have been determined based on the estimated capital and operational needs of the Group.

The above caps for the fees and commissions payable for the provision of fee-based and commission-based financial services by CEC Finance have been determined based on the estimated demand of the fee-based and commission-based financial services provided by CEC Finance and the fees and commissions payable for such services.

### REASONS FOR AND BENEFITS OF THE PROPOSED TRANSACTIONS

The Board believes that the Shanghai Huahong Acquisition and the entry into the 2015-2018 Business Services Agreement and the 2015-2018 Financial Services Agreement are in line with the development strategies of the Group, and will bring long-term and strategic benefits to the Group, including but not limited to, the following:

#### **The Shanghai Huahong Acquisition**

1. With the launch of new supportive policies, the integrated circuit industry holds great future development potential in the PRC. The Shanghai Huahong Acquisition will enable the Group to be well positioned to swiftly capitalise on the enormous market opportunities created by the development of the integrated circuit industry.

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## LETTER FROM THE BOARD

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2. The Group plans to step up its efforts on expanding the business in the horizon of the design of contactless and dual-interface integrated circuit chip solutions and services. Huahong is a leading supplier of contactless public transport and electronic travel document solutions and services. Huahong is also well positioned to tap into the PRC dual-interface financial security solutions and services market, which at present imported most of the integrated circuit chips for bank cards from overseas. Following the Shanghai Huahong Acquisition, there will be tremendous synergies between the business of Huahong and the Group. The Shanghai Huahong Acquisition represents a significant strategic move by the Group in broadening its business coverage, and in capturing a dominant position in the PRC contactless and dual-interface integrated circuit chip markets.
3. As both Huahong and Huada Electronics are engaged in the design of integrated circuit chips, the Shanghai Huahong Acquisition will bring the following benefits to the integrated circuit business of the Group:
  - (i) improve overall productivity of the Group through the integration of existing technologies of Huahong and Huada Electronics and the joint development and application of new technologies, which will save costs related to research and development;
  - (ii) improve management efficiency and strategic decision making of the Group by leveraging on the combined experience of the management teams of Huahong and Huada Electronics in the design of integrated circuit chips;
  - (iii) enhance the bargaining power of procurement of the Group through collaboration with Huahong; and
  - (iv) improve the Group's market coverage and presence through Huahong's integrated circuit chip offerings and its current and prospective customer base.

The Directors are of the view that the terms of the Shanghai Huahong Acquisition Agreements are fair and reasonable and in the interests of the Company and the Shareholders as a whole.

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## LETTER FROM THE BOARD

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### **2015-2018 Business Services Agreement and 2015-2018 Financial Services Agreement**

Following the completion of the Huada Semiconductor Acquisition, Huahong will become an indirect subsidiary of the Company. Huahong has on-going transactions with the CEC Group which are similar to those contemplated under the 2013-2016 Business Services Agreement and the 2013 Financial Services Agreements in its ordinary and usual course of business. These transactions will, after the completion of the Huada Semiconductor Acquisition, become continuing connected transactions of the Company. In order to streamline the continuing connected transactions between members of the Group (including Huahong after the completion of the Huada Semiconductor Acquisition) and members of the CEC Group, the Company entered into the 2015-2018 Business Services Agreement with CEC and the 2015-2018 Financial Services Agreement with CEC Finance which will, upon taking effect, supersede the 2013-2016 Business Services Agreement and the 2013 Financial Services Agreements, respectively.

#### ***(1) 2015-2018 Business Services Agreement***

The Group is engaged in the design of integrated circuit chips. The CEC Group provides products processing, testing and assembling services for the production of the Group's products and supplies raw materials, modules, software and equipment to the Group for its research and development purposes. The CEC Group is also a customer of the Group. The transactions contemplated under the 2015-2018 Business Services Agreement are, therefore, vital and integral to the business operations of the Group.

The Directors are of the view that the transactions contemplated under the 2015-2018 Business Services Agreement will be conducted on normal commercial terms (or better to the Group) and in the ordinary and usual course of business of the Group and that the terms of the 2015-2018 Business Services Agreement and the proposed caps are fair and reasonable and in the interests of the Company and the Shareholders as a whole.

#### ***(2) 2015-2018 Financial Services Agreement***

CEC Finance is a non-banking financial institution approved and regulated by the PBOC and the CBRC. CEC Finance was established for the purpose of enhancing the centralised management of funds within the CEC Group and for improving the fund utilisation efficiency of the CEC Group as a whole. CEC Finance is permitted to provide various financial services such as deposit services, loan services, finance leasing and investment services to the CEC Group.

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## LETTER FROM THE BOARD

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The main reasons and advantages for utilising the financial services provided by CEC Finance are as follows:

- (i) The interest rates on deposits and financial assistance offered by CEC Finance to the Group will be no less favourable than those offered by other domestic commercial banks. The fees and commissions for the fee-based and commission-based financial services provided by CEC Finance will not be higher than those charged by other domestic commercial banks or financial institutions.
- (ii) CEC Finance is regulated by the PBOC and the CBRC and provides its services in accordance and in compliance with the rules and operational requirements of these regulatory authorities.
- (iii) The Group expects to benefit from CEC Finance's better understanding of the operations of the Group which will allow expedient and efficient delivery of services. The Group also expects that as an intra-group service provider, CEC Finance will generally have more efficient communication channels with the Group as compared with other domestic commercial banks or financial institutions.
- (iv) The 2015-2018 Financial Services Agreement will provide the Group with the right and flexibility, which it may choose from different kinds of financial assistance provided by CEC Finance and secure additional and stable financing for its operations.

The Directors are of the view that the transactions contemplated under the 2015-2018 Financial Services Agreement will be conducted on normal commercial terms (or better to the Group) and in the ordinary and usual course of business of the Group and that the terms of the 2015-2018 Financial Services Agreement and the proposed caps are fair and reasonable and in the interests of the Company and the Shareholders as a whole.

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## LETTER FROM THE BOARD

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### RISK FACTORS

#### Risks relating to the business of Huahong

##### ***The business of Huahong is dependent on the information technology sector in the PRC***

The business of Huahong depends on the growth of the information technology sector in the PRC, particularly the electronic information technology sector, which is the driving force behind the demand for integrated circuit chips. Although the information technology sector is demonstrating a growing trend which is in part supported by favourable government policies, any negative trend in the information technology sector or other restrictive policies may materially and adversely affect the business, financial condition and results of operation of Huahong.

##### ***Huahong's results of operation substantially depend on its ability to continue to execute its business strategy and development plan after the completion of the Shanghai Huahong Acquisition***

The PRC integrated circuit market is highly competitive with relatively short product cycles, and significantly affected by the policies of the government. Huahong's results of operation substantially depend on the successful execution of its business strategy and development plan to maintain its leading position in the design of integrated circuit chip sector in the PRC.

Huahong may face challenges in implementing its strategies, and its ability to achieve its goals may be adversely affected by various factors, some of which are beyond its control. If Huahong is not able to execute its business strategy and development plan after the completion of the Shanghai Huahong Acquisition, its business, financial condition and results of operation may be materially and adversely affected.

##### ***Huahong's success depends on its senior management team***

Huahong's success depends significantly on the continued service of the members of its senior management team who are critical to the development and implementation of its corporate strategy and its continued growth.

There is no assurance that Huahong will be able to retain its senior management team to grow and develop its business after Completion. If Huahong fails to retain its senior management team after Completion, its business, financial condition and results of operation may be materially and adversely affected.

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## LETTER FROM THE BOARD

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### **Risk relating to the Shanghai Huahong Acquisition**

***The Shanghai Huahong Acquisition is subject to regulatory approval by authorities in the PRC***

Completion is conditional upon, amongst other things, the Shanghai Huahong Acquisition Agreements having completed all the necessary approvals and/or filing procedures in the PRC. The relevant approval and filing procedures are subject to various factors some of which are beyond Huada Electronics' control, and Huada Electronics cannot guarantee whether and when the necessary approval and/or filing procedures will be completed. The long-term and strategic development of the Group may be materially and adversely affected if Completion could not take place as a result of the necessary approvals not being granted.

### **INFORMATION ON THE PARTIES**

#### **(a) Information on the Company**

The Company is an investment holding company. The Group is principally engaged in the design and sale of integrated circuit chips, and the development and management of electronic information technology industrial parks.

#### **(b) Information on CEC**

CEC is a state-owned enterprise established under the laws of the PRC. Established in 1989 with the approval of the State Council of the PRC, CEC is a nationwide electronics and information technology conglomerate directly administered by the PRC government. CEC actively focuses on communications, consumer electronics, semi-conductor and software sectors in the PRC.

#### **(c) Information on Huada Electronics**

Huada Electronics is principally engaged in the design and sale of integrated circuit chips.

#### **(d) Information on Huada Semiconductor**

Huada Semiconductor is principally engaged in the design and sale of integrated circuit products.

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## LETTER FROM THE BOARD

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**(e) Information on Huahong Group**

Huahong Group is principally engaged in the design, manufacturing and sale of integrated circuit products.

**(f) Information on CEC Finance**

CEC Finance is a non-banking financial institution approved and regulated by the PBOC and the CBRC. CEC Finance was established for the purpose of enhancing the centralised management of funds within the CEC Group and for improving the fund utilisation efficiency of the CEC Group as a whole.

### LISTING RULES IMPLICATIONS

As at the Latest Practicable Date, CEC was interested in approximately 59.42% of the issued share capital of the Company. CEC is the ultimate controlling shareholder of the Company and is therefore a connected person of the Company under the Listing Rules. Accordingly, the Shanghai Huahong Acquisition constitutes a connected transaction of the Company.

As one or more of the applicable percentage ratios referred to in Chapters 14 and 14A of the Listing Rules for the Shanghai Huahong Acquisition exceed 25% but all of which are less than 100%, the Shanghai Huahong Acquisition constitutes a major transaction and connected transaction of the Company under Chapters 14 and 14A of the Listing Rules respectively and is subject to the reporting, announcement and independent shareholders' approval requirements.

CEC is the ultimate controlling shareholder of the Company and is therefore a connected person of the Company under the Listing Rules. Upon the completion of the Huada Semiconductor Acquisition, the 2015-2018 Business Services Agreement and the transactions thereunder will constitute continuing connected transactions of the Company.

As one or more of the applicable percentage ratios set out in Rule 14.07 of the Listing Rules in respect of the 2015-2018 Business Services Agreement are more than 5%, the 2015-2018 Business Services Agreement and the proposed caps for the transactions thereunder are subject to the reporting, annual review, announcement and independent shareholders' approval requirements under Chapter 14A of the Listing Rules.

CEC Finance is a subsidiary of CEC and is therefore a connected person of the Company under the Listing Rules. Upon the completion of the Huada Semiconductor Acquisition, the 2015-2018 Financial Services Agreement and the transactions thereunder will constitute continuing connected transactions of the Company.

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## LETTER FROM THE BOARD

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As one or more of the applicable percentage ratios set out in Rule 14.07 of the Listing Rules in respect of the 2015-2018 Financial Services Agreement are more than 5% and that the Group may be required to provide security for certain types of financial assistance to be provided by CEC Finance, the 2015-2018 Financial Services Agreement and the proposed caps for the transactions thereunder are subject to the reporting, annual review, announcement and independent shareholders' approval requirements under Chapter 14A of the Listing Rules.

None of the Directors have a material interest in the Shanghai Huahong Acquisition, the 2015-2018 Business Services Agreement and the 2015-2018 Financial Services Agreement. Accordingly, no Director was required to abstain from voting on the relevant board resolutions.

### SGM

A notice convening the SGM to be held at Plaza 1-2, Lower Lobby, Novotel Century Hong Kong, 238 Jaffe Road, Wanchai, Hong Kong on 19 November 2015 at 10:00 a.m. is set out on pages SGM-1 to SGM-4 of this circular. At the SGM, resolutions will be proposed to approve (a) the Shanghai Huahong Acquisition and (b) the 2015-2018 Business Services Agreement and the 2015-2018 Financial Services Agreement and their respective proposed caps. Any connected person, and any Shareholder with a material interest in the transaction and its associates, will not vote. As such, CEC and its associates shall abstain from voting on the resolutions approving (a) the Shanghai Huahong Acquisition and (b) the 2015-2018 Business Services Agreement and the 2015-2018 Financial Services Agreement and their respective proposed caps. Pursuant to Rule 13.39(4) of the Listing Rules, all the above resolutions shall be taken by poll at the SGM.

A form of proxy for use at the SGM is enclosed with this circular. Whether or not you are able to attend the SGM, you are requested to complete the accompanying form of proxy in accordance with the instructions printed thereon and return the same to the Company's branch share registrar and transfer office in Hong Kong, Tricor Abacus Limited at Level 22, Hopewell Centre, 183 Queen's Road East, Wanchai, Hong Kong not later than 48 hours before the time appointed for holding the SGM or any adjournment thereof. Completion and return of the form of proxy will not preclude you from attending and voting in person at the SGM or any adjournment thereof should you so wish.

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## LETTER FROM THE BOARD

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### BOOK CLOSURE PERIOD

Shareholders whose names appear on the register of members of the Company on 19 November 2015 will be entitled to attend and vote at the SGM. The register of members of the Company will be closed from 17 November 2015 to 19 November 2015 (both days inclusive), during which period no transfer of shares of the Company will be registered.

In order to be entitled to attend and vote at the SGM, all share certificates with completed transfer forms must be lodged with the Company's branch share registrar and transfer office in Hong Kong, Tricor Abacus Limited at Level 22, Hopewell Centre, 183 Queen's Road East, Wanchai, Hong Kong not later than 4:30 p.m. on 16 November 2015.

### RECOMMENDATION

Based on the relevant information disclosed herein, the Directors are of the view that (a) the terms of the Shanghai Huahong Acquisition Agreements are fair and reasonable and in the interests of the Company and the Shareholders as a whole, (b) the transactions contemplated under the 2015-2018 Business Services Agreement and the 2015-2018 Financial Services Agreement will be conducted on normal commercial terms (or better to the Group) and in the ordinary and usual course of business of the Group and that the terms of the 2015-2018 Business Services Agreement and the 2015-2018 Financial Services Agreement and their respective proposed caps are fair and reasonable and in the interests of the Company and the Shareholders as a whole. Accordingly, the Directors recommend the Independent Shareholders to vote in favour of the resolutions to be proposed at the SGM in relation to (a) the Shanghai Huahong Acquisition and (b) the 2015-2018 Business Services Agreement and the 2015-2018 Financial Services Agreement and their respective proposed caps.

### FURTHER INFORMATION

Your attention is also drawn to the financial and general information set out in the appendices to this circular.

Yours faithfully,

For and on behalf of the Board

**China Electronics Corporation Holdings Company Limited**

**Rui Xiaowu**

*Chairman*

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## LETTER FROM THE INDEPENDENT BOARD COMMITTEE

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**CHINA ELECTRONICS CORPORATION HOLDINGS COMPANY LIMITED**

**中國電子集團控股有限公司\***

*(Incorporated in the Cayman Islands and continued in Bermuda with limited liability)*

**(Stock Code: 00085)**

27 October 2015

*To the Independent Shareholders*

Dear Sir or Madam,

**MAJOR TRANSACTION AND CONNECTED TRANSACTION  
IN RELATION TO  
THE ACQUISITION OF A 95.64% EQUITY INTEREST IN HUAHONG**

**CONTINUING CONNECTED TRANSACTIONS  
2015-2018 BUSINESS SERVICES AGREEMENT WITH CEC  
AND  
2015-2018 FINANCIAL SERVICES AGREEMENT WITH  
CEC FINANCE**

We refer to the circular of the Company dated 27 October 2015 (the “Circular”), of which this letter forms part. Capitalised terms used in this letter shall have the same meanings as those defined in the Circular, unless the context otherwise requires.

In compliance with the Listing Rules, we have been appointed to advise the Independent Shareholders in relation to the terms of the Shanghai Huahong Acquisition Agreements, and the 2015-2018 Business Services Agreement and the 2015-2018 Financial Services Agreement and their respective proposed caps. In this connection, Altus Capital has been appointed as the independent financial adviser to advise on these matters.

\* For identification purpose only

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## LETTER FROM THE INDEPENDENT BOARD COMMITTEE

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Your attention is drawn to the “Letter from the Board” set out on pages 7 to 40 of the Circular which contains, inter alia, information about the terms of the Shanghai Huahong Acquisition Agreements, and the 2015-2018 Business Services Agreement and the 2015-2018 Financial Services Agreement and their respective proposed caps, the “Letter from Altus Capital” set out on pages 43 to 92 of the Circular which contains the advice from Altus Capital in respect of the terms of the Shanghai Huahong Acquisition Agreements, and the 2015-2018 Business Services Agreement and the 2015-2018 Financial Services Agreement and their respective proposed caps, and the additional information set out in the appendices thereto.

We, having considered the terms of the Shanghai Huahong Acquisition Agreements, and the 2015-2018 Business Services Agreement and the 2015-2018 Financial Services Agreement and their respective proposed caps and having taken into account the principal factors and reasons considered by Altus Capital as stated in its letter of advice, consider that the terms of the Shanghai Huahong Acquisition Agreements, and the 2015-2018 Business Services Agreement and the 2015-2018 Financial Services Agreement and their respective proposed caps are fair and reasonable and in the interests of the Company and the Shareholders as a whole. Accordingly, we recommend the Independent Shareholders to vote in favour of the ordinary resolutions to be proposed at the SGM in relation to the Shanghai Huahong Acquisition, and the 2015-2018 Business Services Agreement and the 2015-2018 Financial Services Agreement and their respective proposed caps, as detailed in the notice of SGM set out on pages SGM-1 to SGM-4 of the Circular.

Yours faithfully,

Independent Board Committee

**Chan Kay Cheung**

**Qiu Hongsheng**

**Chow Chan Lum**

*Independent non-executive Directors*

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## LETTER FROM ALTUS CAPITAL

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*The following is the text of a letter of advice from Altus Capital to the Independent Board Committee and the Independent Shareholders in respect of the Shanghai Huahong Acquisition Agreements and the transactions contemplated thereunder, the 2015-2018 Business Services Agreement, 2015-2018 Financial Services Agreement, the transaction contemplated under each of the aforesaid services agreements and the proposed caps for the transactions contemplated under the 2015-2018 Business Services Agreement and the 2015-2018 Financial Services Agreement, which has been prepared for the purpose of incorporation in this circular.*

### ALTUS CAPITAL LIMITED

21 Wing Wo Street  
Central, Hong Kong

27 October 2015

*The Independent Board Committee and the Independent Shareholders*  
China Electronics Corporation Holdings Company Limited  
Room 3403, 34th Floor  
China Resources Building  
26 Harbour Road  
Wanchai, Hong Kong

Dear Sirs,

**MAJOR TRANSACTION AND CONNECTED TRANSACTION  
IN RELATION TO THE ACQUISITION OF  
A 95.64% EQUITY INTEREST IN HUAHONG**

**CONTINUING CONNECTED TRANSACTIONS  
2015-2018 BUSINESS SERVICES AGREEMENT WITH CEC  
AND  
2015-2018 FINANCIAL SERVICES AGREEMENT WITH  
CEC FINANCE**

### INTRODUCTION

We refer to our appointment as the independent financial adviser to advise the Independent Board Committee and the Independent Shareholders in respect of the Shanghai Huahong Acquisition Agreements and the transactions contemplated thereunder, the transactions contemplated under the 2015-2018 Business Services Agreement as well as 2015-2018 Financial

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## LETTER FROM ALTUS CAPITAL

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Services Agreement and the proposed caps relating thereto. Details of (i) the Shanghai Huahong Acquisition, and (ii) the transactions contemplated under the 2015-2018 Business Services Agreement as well as the 2015-2018 Financial Services Agreement (the “**Continuing Connected Transactions**”) and the proposed caps relating thereto are set out in the “Letter from the Board” contained in the circular of the Company dated 27 October 2015 (the “**Circular**”), of which this letter forms part. Terms used in this letter shall have the same meaning as those defined in the Circular unless the context required otherwise.

On 26 June 2015, Huada Electronics, a wholly-owned subsidiary of the Company, entered into the Huada Semiconductor Agreement and the Individual Vendor Agreement(s) respectively pursuant to which Huada Electronics conditionally agreed to acquire (i) 73.43% equity interest in Huahong from Huada Semiconductor; and (ii) an aggregate of 9.95% equity interest in Huahong from Individual Vendors. On the same day, Huada Electronics entered into the Huahong Group Agreement with Huahong Group. This was a preliminary agreement with regard to the proposed transfer of 7.62% equity interest in Huahong from Huahong Group to Huada Electronics.

Incidental to the Huada Semiconductor Acquisition, on 26 June 2015 the Company entered into (i) the 2015-2018 Business Services Agreement with CEC, pursuant to which the CEC Group will provide product processing, testing and assembling services to the Group and purchase integrated circuit cards and smart cards modules and chips from the Group and the Group will purchase raw materials, modules, software and equipment from the CEC Group; and (ii) the 2015-2018 Financial Services Agreement with CEC Finance, pursuant to which CEC Finance will provide a range of financial services to the Group.

On 27 August 2015, Huada Electronics entered into the Supplemental Huahong Group Agreement and the Remaining Shareholders Agreement(s) respectively. The Supplemental Huahong Group Agreement is to further determine certain terms under the Huahong Group Agreement, including, among other things, the amount of consideration, conditions precedent and the terms of completion. Pursuant to the Remaining Shareholders Agreement(s), Huada Electronics conditionally agreed to acquire an aggregate of 4.64% equity interest in Huahong from the Individual Vendors.

In summary, upon completion of the Shanghai Huahong Acquisition Agreements, the Company will hold an aggregate of 95.64% equity interest in Huahong.

As at the Latest Practicable Date, CEC, which was interested in approximately 59.42% and approximately 77.02% of the issued capital of the Company and Huahong respectively, was the ultimate controlling shareholder of the Company and Huahong and hence a connected person of the Company and Huahong under Chapter 14A of the Listing Rules. Moreover, one or more of the applicable percentage ratios referred to in Chapters 14 and 14A of the Listing Rules for the Shanghai Huahong Acquisition exceed 25% but all of which are less than 100%. Accordingly, the

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## LETTER FROM ALTUS CAPITAL

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Shanghai Huahong Acquisition constitutes a major transaction as well as connected transaction of the Company under Chapter 14 and 14A of the Listing Rules respectively and is subject to the reporting, announcement and independent shareholders' approval requirements.

Further, upon the completion the Huada Semiconductor Acquisition, as CEC is a connected person of the Company under the Listing Rules (as explained above), the 2015-2018 Business Services Agreement and the transactions thereunder will constitute continuing connected transactions for the Company. In this regard, as one or more of the applicable percentage ratios set out under Rule 14.07 of the Listing Rules in respect of the 2015-2018 Business Services Agreement are more than 5%, the 2015-2018 Business Services Agreement and the proposed caps for the transactions thereunder are subject to the reporting, annual review, announcement and independent shareholders' approval requirements under Chapter 14A of the Listing Rules.

As at the Latest Practicable Date, CEC Finance was a subsidiary of CEC and was therefore a connected person of the Company under the Listing Rules. As such, the 2015-2018 Financial Services Agreement and the transactions thereunder will constitute continuing connected transactions of the Company. In this respect, as one or more of the applicable percentage ratios set out under Rule 14.07 of the Listing Rules in respect of the 2015-2018 Financial Services Agreement are more than 5% and that the Group may be required to provide security for certain types of financial assistance to be provided by CEC Finance, the 2015-2018 Financial Services Agreement and the proposed caps for the transactions thereunder are subject to the reporting, annual review, announcement and independent shareholders' approval requirements under Chapter 14A of the Listing Rules.

### THE INDEPENDENT BOARD COMMITTEE

The Independent Board Committee, comprising all the independent non-executive Directors, namely, Mr. Chan Kay Cheung, Mr. Qiu Hongsheng and Mr. Chow Chan Lum, has been established to consider the Shanghai Huahong Acquisition, the Continuing Connected Transactions and the proposed caps relating thereto, and to give advice and recommendation to the Independent Shareholders as to whether the Shanghai Huahong Acquisition, the Continuing Connected Transactions and the proposed caps relating thereto are fair and reasonable and in the interests of the Company and the Shareholders as a whole and on how to vote on the resolutions to be proposed at the SGM.

As the independent financial adviser to the Independent Board Committee and the Independent Shareholders, our role is to give an independent opinion to the Independent Board Committee and the Independent Shareholders as to (i) whether the Shanghai Huahong Acquisition and the Continuing Connected Transactions and the proposed caps relating thereto are in the ordinary and usual course of business of the Group and are in the interests of the Company and the Shareholders as a whole; (ii) whether the respective terms of the Shanghai Huahong Acquisition and

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the Continuing Connected Transactions are on normal commercial terms and are fair and reasonable so far as the Independent Shareholders are concerned; (iii) whether the proposed caps with regard to the Continuing Connected Transactions have been fairly and reasonably arrived at; and (iv) how the Independent Shareholders should vote in respect of the resolutions relating to the Shanghai Huahong Acquisition and the Continuing Connected Transactions and the respective proposed caps relating thereto at the SGM.

### **BASIS OF OUR OPINION**

In formulating our opinion, we have relied on the statements, information, opinions and representations contained or referred to in the Circular and/or provided to us by the Company, the Directors and the management of the Company (the “**Management**”). We have assumed that all statements, information, opinions and representations contained or referred to in the Circular and/or provided to us were true, accurate and complete at the time they were made and continued to be so as at the date of the Circular.

We have no reason to believe that any statements, information, opinions or representations relied on by us in forming our opinion is untrue, inaccurate or misleading, nor are we aware of any material facts the omission of which would render the statements, information, opinions or representations provided to us untrue, inaccurate or misleading. We have assumed that all the statements, information, opinions and representations for matters relating to the Group contained or referred to in the Circular and/or provided to us by the Company, the Directors and the Management have been reasonably made after due and careful enquiry. We have relied on such statements, information, opinions and representations and have not conducted any independent investigation into the business, financial conditions and affairs or the future prospects of the Group.

### **PRINCIPAL FACTORS AND REASONS CONSIDERED**

#### **(I) THE SHANGHAI HUAHONG ACQUISITION**

In arriving at our opinion and recommendation, we have taken into account the following principal factors and reasons.

##### **1. Background information**

###### ***1.1 Principle business of the Company and its subsidiaries***

The Company is an investment holding company. The Group is principally engaged in the design and sale of integrated circuit chips and the development and management of electronic information technology industrial parks.

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On 5 July 2013, the Company purchased 100% equity interest in CEC Technology which holds investments that are primarily engaged in the development and management of industrial parks in the PRC. The transaction was completed on 26 June 2014 and since the industrial parks were still in their initial development stage, 99% of the revenue of the Group for the years ended 31 December 2013 and 2014 and for the six months ended 30 June 2015 was generated from the design and sale of integrated circuit chips.

### **1.2 Historical financial information of the Group**

The following table sets out selected items in the consolidated financial statements of the Group for the two years ended 31 December 2014 and for the six months ended 30 June 2015 as extracted from the Company's annual report for the year ended 31 December 2014 (the "**2014 Annual Report**") and the interim report for the six months ended 30 June 2015 (the "**2015 Interim Report**").

|                                                                     | Year ended<br>31 December |                   | Six months ended<br>30 June |                   |
|---------------------------------------------------------------------|---------------------------|-------------------|-----------------------------|-------------------|
|                                                                     | 2013                      | 2014              | 2014                        | 2015              |
|                                                                     | HK\$'000                  | HK\$'000          | HK\$'000                    | HK\$'000          |
|                                                                     | (Restated)                | (Audited)         | (Restated)                  | (Unaudited)       |
| Revenue                                                             | 1,321,606                 | 1,357,062         | 703,664                     | 639,558           |
| Research and development costs                                      | 213,002                   | 214,187           | 102,975                     | 100,102           |
| Government grants ( <i>Note 1</i> )                                 | 31,320                    | 71,533            | 27,491                      | 47,036            |
| Finance costs                                                       | 24,991                    | 205,723           | 99,425                      | 99,771            |
|                                                                     |                           | ( <i>Note 2</i> ) | ( <i>Note 2</i> )           | ( <i>Note 2</i> ) |
| Profit before taxation                                              | 347,863                   | 216,174           | 143,456                     | 178,001           |
| Profit for the year/period attributable<br>to owners of the Company | 291,966                   | 170,108           | 109,734                     | 149,092           |

*Notes:*

1. This represents government grants that are recognised as other income which are granted by and received from local government authorities to finance the Group's research and development projects.
2. This represents the net finance cost arising from the issuance of a unsecured bond on 16 January 2014 in the sum of RMB2,750 million and carrying an interest rate of 4.70% per annum.

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|                                              | As at 31 December |           | As at<br>30 June |
|----------------------------------------------|-------------------|-----------|------------------|
|                                              | 2013              | 2014      | 2015             |
|                                              | HK\$'000          | HK\$'000  | HK\$'000         |
|                                              | (Restated)        | (Audited) | (Unaudited)      |
| Cash and cash equivalents                    | 791,781           | 534,134   | 617,393          |
| Short-term deposits and investments          | –                 | 3,259,010 | 2,933,924        |
| Total assets                                 | 2,623,028         | 6,726,268 | 6,821,376        |
| Unsecured corporate bonds                    | –                 | 3,436,724 | 3,449,493        |
| Deferred government grants ( <i>Note 1</i> ) | 181,342           | 137,742   | 100,154          |
| Bank and other borrowings ( <i>Note 2</i> )  | 508,547           | 1,332,462 | 1,255,548        |
| Total liabilities                            | 1,411,212         | 5,624,438 | 5,623,584        |
| Net asset value                              | 1,211,816         | 1,101,830 | 1,197,792        |

*Source: 2014 Annual Report and 2015 Interim Report*

*Notes:*

1. This mainly represents various government grants granted by and received from local government authorities to finance various research and development projects conducted by the Group. These government grants will be recognised as income over the period necessary to match with the cost that they are intended to compensate.
2. This represents the total amount of bank and other borrowings.

*For the year ended 31 December 2014*

Total revenue of the Group increased from approximately HK\$1,321.6 million in 2013 to approximately HK\$1,357.1 million in 2014, representing a slight increase of approximately 2.7%. The integrated circuit design operation contributed to approximately 99.0% and 99.6% of the total revenue of the Group for the year ended 31 December 2013 and 2014 respectively. According to the 2014 Annual Report, the average selling prices of integrated circuit chips products in 2014 were generally lower when compared with those of 2013 due to the intensification of market price competition. The fall in average selling prices of integrated circuit chips products was compensated by an approximately 52.3% rise in overall sales volume as a result of the Group's effort in expanding the market share of its products.

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During the year ended 31 December 2014, the Group incurred research and development costs of approximately HK\$214.2 million (2013: HK\$213.0 million). The Group's research and development was primarily focused on the Europay, Mastercard and Visa ("EMV") card, mobile payment card, radio frequency identification ("RFID") and global navigation system chip products. Such research and development costs represented approximately 15.8% (2013: 16.1%) of the Group's total revenue in 2014.

As a measure to incentivise enterprises to invest in research and development, the Group obtained grants from the government of the PRC and recognised as income over the period necessary to match with the cost that they are intended to compensate. Such amount of other income increased from approximately HK\$26.1 million in 2013 to approximately HK\$62.6 million in 2014, representing an increase of approximately 139.8% due to the variations in government subsidies for research and development costs incurred during that year.

The Group recorded profit attributable to owners of the Company of approximately HK\$170.1 million for the year ended 31 December 2014, representing a decrease of approximately 41.7% compared to 2013. Such decrease was mainly attributable to the absence of a one-off gain of approximately HK\$120.0 million arising from the completion of disposal of 50% equity interest in a joint venture in the year ended 31 December 2013 and an increase in finance costs of approximately HK\$180.7 million arising from the issuance of an unsecured bond on 16 January 2014 in the sum of RMB2,750 million and carrying an interest at the rate of 4.70% per annum.

The Group generally finances its working capital and funding requirements through internal resources, bank and other borrowings and issuance of corporate bonds. As at 31 December 2014, the Group's cash and cash equivalents amounted to approximately HK\$534.1 million (2013: HK\$791.8 million) whilst there were total bank and other borrowings of approximately HK\$1,332.5 million (2013: HK\$508.5 million) and undrawn committed borrowing facilities available to the Group of approximately HK\$937.9 million (2013: HK\$432.3 million). The Group also made short-term deposits at banks or other financial institutions in 2014 in the sum of approximately HK\$3,259.0 million and carrying an interest at the rate of 2.45% per annum. The Group's gearing ratio (calculated as total liabilities over total assets) increased to approximately 83.6%, as compared with approximately 53.8% as at 31 December 2013 due to the issuance of the abovementioned unsecured bonds and new bank and other borrowings during the year ended 31 December 2014.

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*For the six months ended 30 June 2015*

Total revenue of the Group for the six months ended 30 June 2015 amounted to approximately HK\$639.6 million (2014: HK\$703.7 million), representing a decrease of approximately 9.1% as compared to the corresponding period in 2014. The integrated circuit design operation continued to contribute the majority of the Group's revenue for the six months ended 30 June 2014 and 2015 respectively. According to the 2015 Interim Report, the average selling prices of integrated circuit chips products were lower than the corresponding period in 2014 due to the further intensification of market competition in 2015. The fall in average selling prices of integrated circuit chips products was compensated by an approximately 38.7% rise in the overall sales volume as a result of the Group's continued effort in expanding the market share of its products.

During the six months ended 30 June 2015, the Group incurred research and development costs of approximately HK\$100.1 million (2014: HK\$103.0 million). The Group's research and development continued to focus on the EMV card, mobile payment card, RFID and global navigation system chip products. Such research and development costs represented approximately 15.8% (2014: 14.7%) of the Group's total revenue for the six months ended 30 June 2015.

As a measure to incentivise enterprises to invest in research and development, the Group obtained grants from the government of the PRC and recognised as income over the period necessary to match with the cost that they are intended to compensate. Such amount increased to approximately HK\$47.0 million in the six months ended 30 June 2015, representing an increase of approximately 71.1% due to the variations in government subsidies for research and development costs incurred during that period.

The Group recorded profit attributable to owners of the Company of approximately HK\$149.1 million (2014: HK\$109.7 million) for the six months ended 30 June 2015, representing an increase of approximately 35.9% compared to the corresponding period in 2014. Such increase was principally attributable to the Group's effort in cost control, the increase in other income and gains (net) and the Group's associate generated profit which enabled the Group to share its positive result of approximately HK\$12.7 million as opposed to share a loss of approximately HK\$3.9 million in the corresponding period in 2014.

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The Group generally finances its working capital and funding requirements through internal resources, bank and other borrowings and issuance of corporate bonds. As at 30 June 2015, the Group's cash and cash equivalents amounted to approximately HK\$617.4 million (as at 31 December 2014: HK\$534.1 million), whilst there were total bank and other borrowings of approximately HK\$1,255.5 million (as at 31 December 2014: HK\$1,332.5 million) and undrawn committed borrowing facilities available to the Group of approximately HK\$697.3 million (as at 31 December 2014: HK\$937.9 million). The Group also made short-term deposits at banks or other financial institutions in the sum of approximately HK\$2,933.9 million as at 30 June 2015 (as at 31 December 2014: HK\$3,259.0 million). The Group's gearing ratio (calculated as total liabilities over total assets) as at 30 June 2015 of approximately 82.4% remained at similar level as at 31 December 2014 of approximately 83.6%.

### ***1.3 Prospects of the Group***

As stated in the 2014 Annual Report and 2015 Interim Report, 2014 was a challenging year to the Group due to intense market competition in pricing. During the first half of 2015, market competition in pricing for integrated circuit chips remained severe.

Going forward, the Group's integrated circuit chips business will continue to face pricing pressure and, in turn, may exert pressure to the growth of this business of the Group. However, in view of the Group's leading position in the integrated circuit chips industry in the PRC, and the favorable policies that are being launched by the government of the PRC to develop the integrated circuit chips industry (as described in the paragraph headed "1.7 Prospects of Huahong" below), the Group will continue to adhere to its independent innovation development strategy, increase its investments in science and technology, and actively expand into new smart card application business such as financial security and other chip design segments.

### ***1.4 Information on CEC***

CEC is a state-owned enterprise established under the laws of the PRC. Established in 1989 with the approval of the State Council of the PRC, CEC is a nationwide electronics and information technology conglomerate directly administered by the government of the PRC. CEC actively focuses on communications, consumer electronics, semi-conductor and software sectors in the PRC.

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## LETTER FROM ALTUS CAPITAL

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### 1.5 Information on Huahong

Huahong was established in 1998 under the laws of the PRC. It is an industrial leader in the design of the integrated circuit sector in the PRC. Huahong also focuses on providing customers with system solutions to address their business and operation challenges. Please refer to the paragraph headed “Information on Huahong” in the “Letter from the Board” for further information.

The shareholding structure of Huahong prior to Completion is set out in the paragraph headed “Shareholding structure of Huahong” in the “Letter from the Board” of the Circular.

### 1.6 Historical financial information of Huahong

Set out below is a summary of the audited financial information of Huahong for the three years ended 31 December 2014 and the four months ended 30 April 2015 as extracted from “Accountant’s report of Huahong” sets out in Appendix III to the Circular.

|                                                    | Year ended<br>31 December |         |         | Four months ended<br>30 April |         |
|----------------------------------------------------|---------------------------|---------|---------|-------------------------------|---------|
|                                                    | 2012                      | 2013    | 2014    | 2014                          | 2015    |
|                                                    | RMB'000                   | RMB'000 | RMB'000 | RMB'000                       | RMB'000 |
|                                                    |                           |         |         | (Unaudited)                   |         |
| Revenue                                            | 552,605                   | 479,127 | 457,169 | 132,766                       | 146,368 |
| Research and development costs                     | 96,855                    | 104,575 | 114,557 | 35,823                        | 37,029  |
| Other income – government grants ( <i>Note 1</i> ) | 23,419                    | 47,172  | 63,802  | 1,169                         | 14,050  |
| Profit/(loss) for the year/period                  | 35,085                    | 64,238  | 56,069  | (2,752)                       | (2,261) |

|                                              | As at<br>31 December |         |         | As at<br>30 April |         |
|----------------------------------------------|----------------------|---------|---------|-------------------|---------|
|                                              | 2012                 | 2013    | 2014    | 2014              | 2015    |
|                                              | RMB'000              | RMB'000 | RMB'000 | RMB'000           | RMB'000 |
| Cash and cash equivalent                     | 378,987              | 292,737 | 215,021 | 134,338           |         |
| Trade and other receivables                  | 269,086              | 235,906 | 236,368 | 288,292           |         |
| Total asset                                  | 838,390              | 797,428 | 652,004 | 629,589           |         |
| Deferred government grants ( <i>Note 1</i> ) | 136,894              | 108,245 | 58,307  | 47,724            |         |
| Total liabilities                            | 376,985              | 319,326 | 307,998 | 287,844           |         |

Source: Accountant’s report of Huahong sets out in Appendix III to the Circular.

Note:

- This mainly represents various government grants granted by and received from local government authorities to finance various research and development projects conducted by the Group. These government grants will be recognised as income over the period necessary to match with the cost that they are intended to compensate.

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## LETTER FROM ALTUS CAPITAL

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Huahong's revenue decreased from approximately RMB552.6 million in 2012 to approximately RMB479.1 million in 2013 to approximately RMB457.2 million in 2014, representing a year-on-year decrease of approximately 13.3% and 4.6% respectively. It is noted that in 2012 there was a disposal of large amount of SIM cards in anticipation of the technology transformation of SIM cards in 2013. As there was no such disposal in 2013, when comparing the revenue of the two financial years in 2012 and 2013, 2013 recorded a lower revenue. The slight decrease in revenue in 2014 was mainly due to a decrease from the sale of identity cards. As the replacement of new identity cards passed its peak in 2013 and returned to a relatively normal level in 2014, the sale of identity cards decreased but the negative impact was off-set by the sale of bank cards in 2014. Revenue increased by approximately 10.2% for the four months ended 30 April 2015 as compared to the corresponding period in 2014. This was mainly due to increase in sale of bank cards in 2015.

Huahong incurred research and development costs of approximately RMB96.9 million, RMB104.6 million and RMB114.6 million for the years ended 31 December 2012, 2013 and 2014 respectively, representing a year-on-year increase of approximately 7.9% and 9.6% respectively. Such research and development costs represented approximately 17.5%, 21.8% and 25.1% of Huahong's revenue for the three years ended 31 December 2012, 2013 and 2014 respectively. For the four months ended 30 April 2015, Huahong incurred research and development costs of approximately RMB37.0 million (2014: RMB35.8 million), representing an increase of approximately 3.4% over the corresponding period in 2014.

Similar to the Group, Huahong obtained grants from the government of the PRC for research and development purpose and recognised them as income over the period necessary to match with the cost that they are intended to compensate. Such amount of other income increased from approximately RMB23.4 million in 2012 to approximately RMB47.2 million in 2013 to approximately RMB63.8 million in 2014, representing a year-on-year increase of approximately 101.7% and 35.2% respectively. For the four months ended 30 April 2015, the amount of other income in this respect was approximately RMB14.1 million as compared to approximately RMB1.2 million recorded during the corresponding period in 2014. The movement in the amount of other income was due to the variations in government subsidies for research and development costs incurred.

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Huahong recorded profit of approximately RMB35.1 million, RMB64.2 million and RMB56.1 million for the each of the year ended 31 December 2012, 2013 and 2014 respectively. The decrease in profit in 2014 as compared to 2013 was mainly attributable to the intensified market price competition in the integrated circuit industry. For the four months ended 30 April 2014 and 2015, Huahong recorded a loss of approximately RMB2.8 million and RMB2.3 million respectively. According to the Management, sales in the first quarter of a calendar year were usually slow due to the festive season. In addition, in view of (i) the intensification of the market competition in pricing in 2014 and continued to face the challenge in 2015, (ii) the substantial research and development costs already incurred for the development of integrated circuit chips products; (iii) the sale of certain types of bank cards has yet to achieve mass economic scale, Huahong recorded loss for the four months ended 30 April 2014 and 2015 respectively.

As at 31 December 2012, 2013 and 2014 and as at 30 April 2015, cash and cash equivalents amounted to approximately RMB379.0 million, RMB292.7 million, RMB215.0 million and RMB134.3 million respectively.

According to the Management, Huahong generally finances its working capital and funding requirements through internal resources. Huahong's gearing ratio (calculated as total liabilities over total equity) as at 31 December 2012, 2013 and 2014 and as at 30 April 2015 was approximately 81.7%, 66.8%, 89.5% and 84.2%.

For more details of the management discussion and analysis of the financial results of Huahong, please refer to Appendix I to the Circular.

### ***1.7 Prospects of Huahong***

2014 was a challenging year to Huahong due to intense market competition in pricing. During the four months ended 30 April 2015, market competition in pricing remained severe. According to our discussions with the Management, under the current market condition, Huahong's integrated circuit chips business has continued to face pricing pressure and, in turn, may exert pressure on the profitability of Huahong. Notwithstanding the aforesaid challenging market condition, Huahong is:

- (i) the only integrated circuit chip design company in the PRC whose self-developed dual-interface integrated circuit chips for security control is accredited with both the Common Criteria Evaluation Assurance Level 4+ Certificate and EMVCo certificate (EMVCo was established to manage, maintain and enhance the EMV Specifications for payment systems);

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## LETTER FROM ALTUS CAPITAL

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- (ii) accredited with the full qualification certificate by UnionPay for its self-developed integrated circuit chips; and
- (iii) the sole PRC supplier of bank cards (at state secret level) for the Industrial and Commercial Bank of China Limited and one of the PRC suppliers of bank cards (at state secret level) for the China Construction Bank Corporation.

In view of (i) the PRC government's promotion of the "Made in China 2025" strategy, whereby it intends to reduce its reliance on the current level of foreign technology and to improve the trade deficit situation in the PRC; (ii) PBOC has an ongoing campaign to replace magnetic stripe bankcards with those embedded with integrated circuit chips from 2015 onwards; and (iii) according to the paper titled "2014年集成電路行業發展回顧及展望" published by the Ministry of Industry and Information Technology of the PRC ("MIIT"), the continuous growth of 4G terminals has led to further demand for integrated chips embedded in SIM cards; the Management expects the demand for smart card chips in travel documents as well as integrated circuit chips embedded in bankcards will continue to grow going forward, whereas the demand for integrated circuit chips in the public transportation and social security sectors will grow though at a relatively slower pace.

Notwithstanding the fact that Huahong recorded a loss for the four months ended 30 April 2015 which in part was caused by the continued intensified market competition in pricing in 2015, we have discussed with the Management and noted that in view of (i) Huahong's leading position in the integrated circuit chips industry in the PRC where, among others, it was named (a) one of the top 10 (in terms of sales) integrated circuit design company in Shanghai in 2014 accredited by 上海市集成電路行業協會 (Shanghai Integrated Circuit Industry Association); and (b) one of the top 10 (in terms of sales) integrated circuit design company in the PRC in 2010 accredited by 中國半導體行業協會 (China Semi-conductor Industry Association) (but it did not rank in the top 10 integrated circuit design companies in the PRC in 2014); (ii) the favorable policies that are being launched by the government of the PRC to develop the integrated circuit chips industry; and (iii) the synergistic benefits to be derived from the Shanghai Huahong Acquisition as described in the paragraph headed "2. Reasons for and benefits of the Shanghai Huahong Acquisition" below, the Management has not observed and does not expect any material adverse change to the business condition of Huahong.

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In addition, the Directors believe and we concur that the collaboration and integration of business between Huahong and the Group through the Shanghai Huahong Acquisition will enable the Enlarged Group to secure a leading position in the integrated circuit chips industry in the PRC (given Huahong's leading position in the integrated circuit chips industry in the PRC as mentioned above and the benefits of the Shanghai Huahong Acquisition described in the paragraph headed "2. Reasons for and benefits of the Shanghai Huahong Acquisition" below), enhance the competitiveness of the Enlarged Group and create a long term sustainable platform for the future growth of the Enlarged Group. It is noted that there are certain risks relating to the business of Huahong and the Shanghai Huahong Acquisition as described in the paragraph headed "Risks factors" in the "Letter from the Board" of the Circular. However, based on our discussion with the Management, they do not foresee issues integrating the business of the Enlarged Group.

### **2. Reasons for and benefits of the Shanghai Huahong Acquisition**

We have reviewed the details as set out in the section under "Reasons for and benefits of the proposed transactions" in the "Letter from the Board" of the Circular.

Taking into account that:

- (i) the recent intensification of market price competition, the Group plans to step up its efforts on expanding the business in the fields of the design of contactless and dual-interface integrated circuit chip solutions and services;
- (ii) Huahong, as a leading supplier of contactless public transport and electronic travel document solutions and services, is well positioned to tap into the PRC dual-interface financial security solutions and services market, a sector which the Group plans to expand into (as described in paragraph headed "1.7 Prospects of Huahong" above);
- (iii) the Shanghai Huahong Acquisition will enable the Group to be well positioned to capitalise on the market opportunities created by the development of the integrated circuit industry which is supported by the new supportive policies of the government of the PRC (as described in paragraph headed "1.7 Prospects of Huahong" above);
- (iv) the Shanghai Huahong Acquisition is expected to enhance operating efficiency of the Group through (1) leveraging on Huahong and the Group's experience and technological expertise; and (2) the efficient use of research and development resources to develop more integrated circuit chips products and to eliminate duplicate investment on the same or similar technology; and

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- (v) the Shanghai Huahong Acquisition is further expected to (1) eliminate direct competition between the two corporations; (2) enhance bargaining power to customers as well as suppliers; (3) increase the Group's overall market share in the integrated circuit chips market; and (4) enlarge the Group's customer portfolio and provide cross-selling opportunities from the complementary existing clientele profile of Huada Electronics and Huahong in terms of geographical coverage in the PRC;

we concur with the Directors' view that the Shanghai Huahong Acquisition is beneficial to the Company and in the interests of the Company and the Shareholders as a whole. In particular, notwithstanding the challenges of Huahong which the Group is also facing similarly and the fact that Huahong recorded a loss during the four months ended 30 April 2015 due to the reasons mentioned in the paragraph headed "1.6 Historical financial information of Huahong" above, we have discussed with the Management and are of the view that the benefits of the Shanghai Huahong Acquisition will, in the long run, (i) enable the Enlarged Group to secure a leading position for both the Group and Huahong in the integrated circuit chips industry in the PRC upon Completion; (ii) enhance the competitiveness of the Enlarged Group; and (iii) create a long term sustainable platform for the future growth of the Enlarged Group, outweigh the current challenges faced by Huahong. We are also of the view that the Shanghai Huahong Acquisition is in line with the strategy of the Group despite the fact that it is not in its ordinary and usual course of business of the Group.

### 3. Terms of Shanghai Huahong Acquisition Agreements

#### 3.1 Consideration

The total aggregate consideration for the Shanghai Huahong Acquisition of RMB717.3 million (equivalent to approximately HK\$909.6 million) represents a price to 2014<sup>1</sup> earnings multiple of 13.4 times and a price to 2014<sup>1</sup> sales multiple of 1.6 times, and was determined after arm's length negotiations among the concerned parties to the Shanghai Huahong Acquisition Agreements having regard to (i) the price-to-earnings ratios ("**P/E Ratio**") and the price-to-sales ratios ("**P/S Ratio**") of companies<sup>2</sup> listed on the Stock Exchange which are engaged in similar businesses as Huahong as an indicative range to determine the consideration, taking into account the discount to the valuation as Huahong given that is an unlisted company; (ii) the historical financial performance of Huahong; (iii) the business prospects of Huahong; and (iv) the potential benefits to the Group after the Completion.

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<sup>1</sup> Based on the audited results of Huahong for the year ended 31 December 2014.

<sup>2</sup> The comparable companies are listed in the paragraph headed "3.1.1 Comparable companies" below.

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The Company expects that the consideration will be satisfied in cash from internal resources and borrowing facilities of the Group.

It is noted that the total assets of Huahong as at 31 December 2014 comprised mainly trade and other receivables and cash and cash equivalents. It is also noted that the total liabilities of Huahong as at 31 December 2014 comprised mainly trade and other payables and deferred government grants. As Huahong is focused on the design of integrated circuit chips, the Management is of the view, and we concur, that to determine the value of Huahong based on its net asset value will not be appropriate as it will not be able to capture the value of its technology and expertise. Despite the price to net book value ratios (“**P/B Ratio**”) of companies<sup>2</sup> listed on the Stock Exchange which are engaged in similar businesses as Huahong is not a commonly used valuation benchmark for the type of business Huahong is engaged in, for information of the Shareholders, we also set out the P/B Ratio in the tables below in the paragraph headed “3.1.1 Comparable companies”.

Moreover, whilst the history of Huahong’s income generated from its existing business in the governmental related sectors (e.g. social security, public transport, identity authentication and electronic travel documents) is sufficiently long to provide a fair and reasonable basis to project the future income stream required for an income-approach valuation; given that the dual-interface financial securities solutions and services market is still under development, the Management is of the view that the information currently available will not be representative to project the future income stream required for an income-approach valuation of this segment of business thereby rendering the income approach inappropriate.

Taking into account the above analysis, the Directors believe and we concur that it is fair and reasonable to determine the consideration for the Shanghai Huahong Acquisition by reference to the market comparables, in particular, companies listed on the Stock Exchange which are engaged in similar business as Huahong.

### **3.1.1 Comparable companies**

Given that it is fair and reasonable to determine the consideration for the Shanghai Huahong Acquisition by reference to the market comparables, we have reviewed the P/E Ratios and P/S Ratios of comparable companies (“**Comparable Companies**”) which are (i) listed on the Stock Exchange; and (ii) are principally engaged in business comparable with that of Huahong. Details are set out in the following table:

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<sup>2</sup> The comparable companies are listed in the paragraph headed “3.1.1 Comparable companies” below.

# LETTER FROM ALTUS CAPITAL

We, based on our best endeavour and as far as we are aware, have identified an exhaustive and complete list of 6 Comparable Companies.

Table 1 - comparing based on the market capitalisation as at 26 June 2015

| Company name<br>(stock code)                                          | Principal business                                                                                                             | Market<br>capitalisation<br>as at |                | Profit<br>attributable to<br>owners of<br>the company | Amount of<br>government<br>grants during<br>the year | Net book<br>value (NAV) | P/S<br>Ratio | P/E<br>Ratio  | Adjusted<br>P/E<br>Ratio | P/B<br>Ratio |
|-----------------------------------------------------------------------|--------------------------------------------------------------------------------------------------------------------------------|-----------------------------------|----------------|-------------------------------------------------------|------------------------------------------------------|-------------------------|--------------|---------------|--------------------------|--------------|
|                                                                       |                                                                                                                                | 26 June 2015                      | Revenue        | (Note 1)                                              |                                                      | (Note 1)                | (Note 2)     | (Note 3)      | (Note 4)                 | (Note 7)     |
|                                                                       |                                                                                                                                | HK\$ (million)                    | HK\$ (million) | HK\$ (million)                                        | HK\$ (million)                                       | HK\$ (million)          | (times)      | (times)       | (times)                  | (times)      |
| Advanced Semiconductor<br>Manufacturing<br>Corporation Limited (3355) | Manufacturing and<br>sale of semiconductors                                                                                    | 1,187.9                           | 1,004.2        | 61.3                                                  | 5.8                                                  | 722.8                   | 1.2          | 19.4          | 21.4                     | 1.6          |
| China Electronics Corporation Holdings<br>Company Limited (0085)      | Design and sale of integrated circuit<br>chips, develop and manage of<br>electronic information technology<br>industrial parks | 8,687.9                           | 1,357.1        | 170.1                                                 | 71.5                                                 | 1,101.8                 | 6.4          | 51.1          | 88.1                     | 7.9          |
| Semiconductor Manufacturing<br>International Corporation (0981)       | Manufacturing of semiconductors                                                                                                | 35,860.0                          | 15,267.2       | 1,185.5                                               | 455.7                                                | 25,632.4                | 2.3          | 30.2          | 49.1                     | 1.4          |
| Shanghai Fudan Microelectronics Group<br>Company Limited (1385)       | Design and sale of integrated circuit<br>products                                                                              | 3,318.8                           | 1,062.8        | 211.5                                                 | 102.9                                                | 741.7                   | 3.1          | 15.7          | 30.6                     | 4.5          |
| Sino-Tech International Holdings<br>Limited (0724)                    | Manufacturing and trading of electronic<br>parts and components                                                                | 1,487.8                           | 599.9          | (40.4)                                                | –                                                    | 31.5                    | 2.5          | –<br>(Note 5) | –<br>(Note 5)            | 47.2         |
| Solomon Systech (International)<br>Limited (2878)                     | Design, develop and sale of integrated<br>circuit products                                                                     | 1,307.8                           | 465.6          | (23.3)                                                | –                                                    | 1,075.0                 | 2.8          | –<br>(Note 5) | –<br>(Note 5)            | 1.2          |
|                                                                       |                                                                                                                                |                                   |                |                                                       |                                                      | <b>Minimum:</b>         | 1.2          | 15.7          | 21.4                     | 1.2          |
|                                                                       |                                                                                                                                |                                   |                |                                                       |                                                      | <b>Mean:</b>            | 3.0          | 29.1          | 47.3                     | 10.6         |
|                                                                       |                                                                                                                                |                                   |                |                                                       |                                                      | <b>Median:</b>          | 2.6          | 24.8          | 39.8                     | 3.1          |
|                                                                       |                                                                                                                                |                                   |                |                                                       |                                                      | <b>Maximum:</b>         | 6.4          | 51.1          | 88.1                     | 47.2         |
| Shanghai Huahong (Group) Company<br>Limited (Note 6)                  |                                                                                                                                |                                   |                |                                                       |                                                      |                         | 1.6          | 13.4          | –<br>(Note 5)            | 2.2          |

Source: Respective annual reports of the Comparable Companies and [www.hkex.com.hk](http://www.hkex.com.hk).

## Notes:

- Refers to the latest published audited figure for the year ended 31 December 2014.
- The P/S Ratios of the Comparable Companies are derived from dividing the market capitalisation as at 26 June 2015 (being the date of the Huada Semiconductor Agreement) by the latest published audited revenue of the Comparable Companies.
- The P/E Ratios of the Comparable Companies are derived from dividing the market capitalisation as at 26 June 2015 (being the date of the Huada Semiconductor Agreement) by the latest published audited profit attributable to owners of the Comparable Companies.
- The adjusted P/E ratios of the Comparable Companies (“Adjusted P/E Ratios”) are derived from dividing the market capitalisation as at 26 June 2015 (being the date of the Huada Semiconductor Agreement) by the latest published audited profit attributable to owners of the Comparable Companies having adjusted for the relevant government grants recognised as income during the relevant financial year.

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5. No P/E Ratio or Adjusted P/E Ratio is presented as the relevant group recorded a loss.
6. The P/S Ratio, P/E Ratio and P/B Ratio are calculated based on the total aggregate consideration for the Shanghai Huahong Acquisition.
7. The P/B Ratio of the Comparable Companies are derived from dividing the market capitalisation as at 26 June 2015 (being the date of Huada Semiconductor Agreement) by the latest published audited net asset value of the Comparable Companies.

Table 2 – comparing based on the market capitalisation as at 20 October 2015 (the latest practicable date for ascertaining certain information prior to the date of this letter)

| Company name<br>(stock code)                                          | Principal business                                              | Market<br>capitalisation<br>as at<br>20 October<br>2015<br><i>HK\$ (million)</i> | Revenue<br>(Note 1)<br><i>HK\$ (million)</i> | Profit<br>attributable to<br>owners of<br>the company<br>(Note 1)<br><i>HK\$ (million)</i> | Amount of<br>government<br>grants during<br>the year | Net book<br>value (NAV)<br>(Note 1)<br><i>HK\$ (million)</i> | P/S<br>Ratio<br>(Note 2)<br>(times) | P/E<br>Ratio<br>(Note 3)<br>(times) | Adjusted<br>P/E<br>Ratio<br>(Note 4)<br>(times) | P/B<br>Ratio<br>(Note 7)<br>(times) |
|-----------------------------------------------------------------------|-----------------------------------------------------------------|----------------------------------------------------------------------------------|----------------------------------------------|--------------------------------------------------------------------------------------------|------------------------------------------------------|--------------------------------------------------------------|-------------------------------------|-------------------------------------|-------------------------------------------------|-------------------------------------|
| Advanced Semiconductor<br>Manufacturing<br>Corporation Limited (3355) | Manufacturing and<br>sale of semiconductors                     | 1,018.2                                                                          | 1,004.2                                      | 61.3                                                                                       | 5.8                                                  | 722.8                                                        | 1.0                                 | 16.6                                | 18.4                                            | 1.4                                 |
| China Electronics Corporation Holdings<br>Company Limited (0085)      | Manufacturing and<br>sale of semiconductors                     | 6,028.7                                                                          | 1,357.1                                      | 170.1                                                                                      | 71.5                                                 | 1,101.8                                                      | 4.4                                 | 35.4                                | 61.2                                            | 4.4                                 |
| Semiconductor Manufacturing<br>International Corporation (0981)       | Manufacturing of semiconductors                                 | 30,562.6                                                                         | 15,267.2                                     | 1,185.5                                                                                    | 455.7                                                | 25,632.4                                                     | 2.0                                 | 25.8                                | 41.9                                            | 1.2                                 |
| Shanghai Fudan Microelectronics Group<br>Company Limited (1385)       | Manufacturing of semiconductors                                 | 1,998.8                                                                          | 1,062.8                                      | 211.5                                                                                      | 102.9                                                | 741.7                                                        | 1.9                                 | 9.5                                 | 18.4                                            | 2.7                                 |
| Sino-Tech International Holdings<br>Limited (0724)                    | Manufacturing and trading of electronic<br>parts and components | 763.7                                                                            | 599.9                                        | (40.4)                                                                                     | –                                                    | 31.5                                                         | 1.3                                 | –<br>(Note 5)                       | –<br>(Note 5)                                   | 24.2                                |
| Solomon Systech (International)<br>Limited (2878)                     | Design, develop and sale of<br>integrated circuit products      | 987.0                                                                            | 465.6                                        | (23.3)                                                                                     | –                                                    | 1,075.0                                                      | 2.1                                 | –<br>(Note 5)                       | –<br>(Note 5)                                   | 0.9                                 |
|                                                                       |                                                                 |                                                                                  |                                              |                                                                                            |                                                      | <b>Minimum</b>                                               | 1.0                                 | 9.5                                 | 18.4                                            | 0.9                                 |
|                                                                       |                                                                 |                                                                                  |                                              |                                                                                            |                                                      | <b>Mean</b>                                                  | 2.1                                 | 21.8                                | 35.0                                            | 6.0                                 |
|                                                                       |                                                                 |                                                                                  |                                              |                                                                                            |                                                      | <b>Median</b>                                                | 1.9                                 | 21.2                                | 30.1                                            | 2.1                                 |
|                                                                       |                                                                 |                                                                                  |                                              |                                                                                            |                                                      | <b>Maximum</b>                                               | 4.4                                 | 35.4                                | 61.2                                            | 24.2                                |
| Shanghai Huahong (Group) Company<br>Limited (Note 6)                  |                                                                 |                                                                                  |                                              |                                                                                            |                                                      |                                                              | 1.6                                 | 13.4                                | –<br>(Note 5)                                   | 2.2                                 |

Source: Respective annual reports of the Comparable Companies and [www.hkex.com.hk](http://www.hkex.com.hk).

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*Notes:*

1. Refers to the latest published audited figure for the year ended 31 December 2014.
2. The P/S Ratios of the Comparable Companies are derived from dividing the market capitalisation as at 20 October 2015 (the latest practicable date for ascertaining certain information prior to the date of this letter) by the latest published audited revenue of the Comparable Companies.
3. The P/E Ratios of the Comparable Companies are derived from dividing the market capitalisation as at 20 October 2015 (the latest practicable date for ascertaining certain information prior to the date of this letter) by the latest published audited profit attributable to owners of the Comparable Companies.
4. The adjusted P/E ratios of the Comparable Companies ("**Adjusted P/E Ratios**") are derived from dividing the market capitalisation as at 20 October 2015 (the latest practicable date for ascertaining certain information prior to the date of this letter) by the latest published audited profit attributable to owners of the Comparable Companies having adjusted for the relevant government grants recognised as income during the relevant financial year.
5. No P/E Ratio or Adjusted P/E Ratio is presented as the relevant group recorded a loss.
6. The P/S Ratio, P/E Ratio and P/B Ratio are calculated based on the total aggregate consideration for the Shanghai Huahong Acquisition.
7. The P/B Ratio of the Comparable Companies are derived from dividing the market capitalisation as at 20 October 2015 (the latest practicable date for ascertaining certain information prior to the date of this letter) by the latest published audited net asset value of the Comparable Companies.

With reference to the tables above, it is observed that the P/E Ratio of Huahong represented by the aggregate consideration falls below the mean and median of P/E Ratios of the Comparable Companies. This is favourable to the Group while we have also noted the fact that Huahong is a non-listed company, whereas all the Comparable Companies are listed companies. As such, Huahong's P/E Ratio may be lower than the Comparable Companies given the lower liquidity of its shares. This should however also be considered in conjunction with the fact that the Group is acquiring majority interest in Huahong and hence a control premium is applicable. Independent Shareholders should also note that the business and financial aspects and prospects of the Comparable Companies may differ to those of Huahong and/or the Enlarged Group. In particular, Comparable Companies will not be experiencing the synergies as mentioned in the paragraph headed "2. Reasons for and benefits of the Shanghai Huahong Acquisition" above between Huada Electronics and Huahong upon Completion.

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We also note that the business of Huahong is principally engaged in the integrated circuit chips industry which as mentioned above enjoys favourable government policies. In particular, the government of the PRC also offers grants to companies in the integrated circuit chips industry, including Huahong to promote investment in research and development. We understand from the Management that grants are generally offered on project basis and with a period of no more than three years. In this regard, we note that other than Solomon Systech (International) Limited and Sino-Tech International Holdings Limited, all Comparable Companies have obtained government grants. The percentage of government grants recognised as income to revenue of the Comparable Companies ranges from 0.1% to 8.3%, whilst Huahong's percentage amounted to 14.0%.

As explained above, due to accounting policies, income in the form of grants from the government is to be recognised over the period necessary to match with the cost they are intended to compensate. As a result, profit of the Comparable Companies during specific year could fluctuate depending on the timing of such recognition. To conduct an analysis without such potential anomalies, we have also considered the P/S Ratio which values the Comparable Companies based on their revenue generating ability which reflects, for example, the extensiveness of the market of their products as well as the stage of development of their products.

As illustrated in the tables above, the P/S Ratio of Huahong represented by the aggregate consideration is within the range of the P/S Ratios of the Comparable Companies and lower than both the mean as well as median of the P/S Ratio of the Comparable Companies. This in itself suggests that the aggregate consideration is favourable to the Group as Huahong is priced at a discount to the Comparable Companies in its sector.

As illustrated in the tables above, the P/B Ratio of Huahong represented by the aggregate consideration is within the range of the P/B Ratios of the Comparable Companies and lower than the mean of the P/B Ratio of the Comparable Companies. The P/B ratio also suggests that the aggregate consideration is favourable to the Group as Huahong is priced at a discount to the Comparable Companies in its sector.

Based on the foregoing, together with the future prospects of Huahong as well as the anticipated synergies between Huada Electronics and Huahong (as discussed in the paragraph headed "Reasons for and benefits of the proposed transactions" in the "Letter from the Board" of the Circular), we concur with the Management's view that the consideration is being fairly and reasonably determined.

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### **3.2 Payment terms**

As described in the “Letter of the Board” of the Circular, the aggregate consideration is RMB717.3 million (equivalent to approximately HK\$909.6 million) is to be funded by internal resources and available uncommitted borrowing facilities. Among which, RMB57.1 million payable under the Supplemental Huahong Group Agreement shall be paid in the following manner:

- (i) Huada Electronics shall transfer the consideration into the nominated account of SUAEE;
- (ii) SUAEE shall complete all procedures required for such equity transfer; and
- (iii) on the date agreed between Huahong Group and Huada Electronics (which shall not be later than the period allowed under the requirements of the state-owned asset administrative management and SUAEE), SUAEE shall transfer the consideration into the bank account nominated by Huahong Group after the completion of the procedures set out in paragraph (ii) above.

The date of the Certificate of Assets and Equity Exchange issued by SUAEE shall be the date of completion of the Huahong Group Acquisition.

The aggregate consideration of RMB660.2 million under the Huada Semiconductor Agreement, the Individual Agreement(s) and the Remaining Shareholders Agreement(s) shall be payable within 5 business days from the date of Completion.

We believe that apart from the Group’s existing available cash there are other alternatives to raise funds to finance the consideration for the Shanghai Huahong Acquisition such as bank borrowings, debt financing or equity fund raising exercises that the Company may consider. Our findings in relation to such alternatives are set out below.

- With regard to debt financing such as bank borrowings or issue of debt securities, we note that debt financing would inevitably incur recurring interest expenses over the entire term of such debt financing. It is noted that, the Group had raised a sum of RMB2,750 million by means of

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the issuance of an unsecured bond on 16 January 2014 and carrying an interest rate of 4.70% per annum. Any additional bank borrowings and/or further issue of debt securities, if successfully raised, will increase financial burden to the Group. As the gearing ratio of the Group as at 30 June 2015 (being the latest practicable date for ascertaining such information based on the published financial data of the Group) was 82.4%, any further increase in debts may exert pressure to the gearing ratio and the certainty of obtaining such borrowing facilities.

- For other equity fund raising exercises such as rights issue or open offer, the timing of completion would likely be longer than that of the subject acquisitions, since rights issue or open offer would involve a period under which the rights issue or open offer are open for acceptance by the Shareholders and in the case of a rights issue, a period for trading of the nil-paid rights. Shareholders' reception to a potential rights issue and/or open offer will also be uncertain, which may potentially create difficulties in the negotiation of an underwriting agreement on terms favourable to the Group. Although equity fund raising exercises by means of placing may be quicker in terms of timing than rights issue or open offer, the Company would still have to incur professional fees and underwriting fees in any event in relation to any placing or rights issue and/or open offer. Lastly, given the recent volatile stock market condition in Hong Kong, it is difficult to gauge market reaction and receptiveness of any equity fund exercise; which, in turn, give rise to additional uncertainty to raise equity funding to finance the acquisition.

As at 30 June 2015, the Group had (i) cash and cash equivalents balance of approximately HK\$617.4 million; and (ii) the aggregate undrawn committed borrowing facilities of approximately HK\$697.3 million. The Group also made short term deposits at banks or other financial institutions in the sum of approximately HK\$2,933.9 million as at 30 June 2015. We have discussed with the Management and noted that taking into account the financial resources available to the Enlarged Group, including the internally generated funds and the available committed banking facilities, the Directors are of the opinion that in the absence of unforeseeable circumstances, the Enlarged Group has available sufficient working capital for its requirements, that is for at least the next 12 months from the date of the Circular and there are no other material capital expenditure requirements in the near term. As such, we are of the view that (i) the Group will be able to settle the consideration without any material adverse impact on its general working capital; and (ii) the consideration to be settled by cash is fair and reasonable.

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Having considered the above and the Group's current financial resources, we are of the view that payment in cash by the Group's internal resources is an appropriate means to finance the Shanghai Huahong Acquisition amongst the financing alternatives.

### **3.3 *Conditions precedent***

Details of the conditions precedent to the Shanghai Huahong Acquisition are set out in the "Letter to the Board" of the Circular. In this connection, we note that regardless of whether the Remaining Shareholders elect to transfer their equity interest in Huahong or not, upon Completion, the Company will obtain over 50% of the equity interest (i.e. a controlling stake) in Huahong, thereby enabling the Group to carry out its strategies as discussed above.

## **4. Possible financial effects**

Upon completion of the proposed Shanghai Huahong Acquisitions, the Company will directly hold 95.64% equity interest in Huahong which will then become a non wholly-owned subsidiary of the Company. Accordingly, the assets, liabilities and financial results of Huahong will be consolidated into the consolidated financial statements of the Group.

### **4.1 *Asset and liabilities***

Based on the unaudited pro forma financial information of the Enlarged Group as set out in Appendix IV to the Circular, the net asset value of the Group is expected to decrease due to the settlement of consideration of approximately HK\$909.6 million in cash. Such negative impact on the Group's net asset value may be off-set by combining the assets and liabilities of Huahong to the Group using the principles of merger accounting as prescribed in Accounting Guideline 5 issued by the HKICPA upon the Completion. As at 30 June 2015, the Group recorded a net assets of approximately HK\$1,197.8 million. Upon Completion, the net assets of the Enlarged Group is expected to be approximately HK\$719.8 million, representing a decrease of approximately 39.9%.

### **4.2 *Gearing ratio and liquidity***

As at 30 June 2015, the Group's gearing ratio, was approximately 82.4% as described in paragraph headed "Historical financial information of the Group" above. Based on the unaudited pro forma financial information as set out in Appendix IV to the Circular and assuming that the Shanghai Huahong Acquisition was completed on 30 June 2015, the Enlarged Group's total liabilities amounted to approximately

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HK\$5,986.9 million and total assets amounted to approximately HK\$6,706.7 million. The gearing ratio of the Enlarged Group would then be approximately 89.3% which is slightly higher than before the completion of the Shanghai Huahong Acquisition.

Notwithstanding the decrease in cash after the payment of Shanghai Huahong Acquisition, the Enlarged Group is expected to have sufficient working capital for at least the next twelve months from the date of the Circular after taking into account (i) the completion of the Shanghai Huahong Acquisition, (ii) the cash flow generated from the operating activities; and (iii) the financial resources currently available to the Enlarged Group including internally generated funds and the available committed borrowing facilities.

### **4.3 Earnings**

The results of Huahong will be consolidated in the consolidated financial statements of the Company upon Completion.

As described in the paragraph headed “Prospects of Huahong” above, 2014 was a challenging year to Huahong due to intense market competition in pricing. During the four months ended 30 April 2015, market competition in pricing remained severe. According to our discussion with the Management, if current market condition persists, Huahong’s integrated circuit chips business may continue to face pricing pressure which in turn, may exert pressure on the profitability of Huahong. However, with the collaboration and integration of business between Huahong and the Group through the Shanghai Huahong Acquisition it will enable the Enlarged Group to secure a leading position of the Group in the integrated circuit industry in the PRC, which in turn, will enhance the competitiveness of the Enlarged Group as well as to improve the operating efficiency of the Enlarged Group (such as the efficient use of research and development resources to develop more integrated circuit chips products and to eliminate duplicate investment on the same or similar technology), allowing the Enlarged Group to better weather any adverse market condition. As a result, following the Completion, it is expected to have positive impact to the profitability of the Enlarged Group.

Notwithstanding the abovementioned negative impact to the net assets and the gearing ratio of the Enlarged Group, we are of the view that the long term benefits set out in the paragraph headed “2. Reasons for and benefits of the Shanghai Huahong Acquisition” above outweigh these effects and we consider that the Shanghai Huahong Acquisition is in the interests of the Company and the Shareholders as a whole.

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### 5. Conclusion for the Shanghai Huahong Acquisition

Having considered the above principal factors and reasons, we are of the view that the (i) Shanghai Huahong Acquisition is in the interests of the Company and the Shareholders as a whole despite that the Shanghai Huahong Acquisition was not in the ordinary and usual course of business of the Group; and (ii) the terms of the Shanghai Huahong Acquisition Agreements and the transactions contemplated thereunder are on normal commercial terms and are fair and reasonable so far as the Independent Shareholders are concerned.

### (II) CONTINUING CONNECTED TRANSACTIONS

In considering whether the proposed caps relating to the Continuing Connected Transactions and the terms of the 2015-2018 Business Services Agreement and the 2015-2018 Financial Services Agreement are fair and reasonable, we have taken into account the principal factors and reasons set out below:

#### 1. Background

##### *1.1 Principal businesses of CEC Finance, the Group, the CEC Group and Huahong*

CEC Finance is a non-banking financial institution approved and regulated by the PBOC and the CBRC. It was established for the purpose of enhancing the centralised management of funds among the CEC Group and for improving the fund utilisation efficiency of CEC Group as a whole.

Please refer to the paragraph headed “Principle business of the Company and its subsidiaries”, “Information on CEC” and “Principal business of Huahong” above for further information on the Group, the CEC Group and Huahong respectively.

##### *1.2 The 2013-2016 Business Services Agreement and 2013-2016 Financial Services Agreement*

On 19 July 2010, the Company entered into the 2010-2013 business services agreement with CEC (“**2010-2013 Business Services Agreement**”). Pursuant to which, CEC Group was to provide products processing, testing and assembling services to the Group and purchase integrated circuit cards, smart cards modules and chips from the Group, whilst the Group will purchase raw materials and modules from CEC Group. On the same day, the Company also entered into a comprehensive financial services agreement with CEC Finance (“**2010-2013 Financial Services Agreement**”), pursuant to which, CEC Finance was to provide a range of financial services to the Group.

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On 7 May 2013, the Company entered into the 2013-2016 Business Services Agreement with CEC and the 2013-2016 Financial Services Agreement with CEC Finance, the terms of which are substantially the same as those prescribed in the 2010-2013 Business Services Agreement and 2010-2013 Financial Services Agreement. Both agreements will expire on 30 June 2016. On 11 October 2013, incidental to the Group's acquisition of 100% equity interest in CEC Technology, the CEC Technology Financial Services Agreement was entered into between CEC Technology and CEC Finance pursuant to which CEC Finance was to provide a range of financial services to CEC Technology. In order to streamline the existing continuing connected transactions contemplated under the abovementioned agreements and to facilitate the Group's operation after the completion of the Huada Semiconductor Acquisition, the Company entered into the 2015-2018 Business Services Agreement and the 2015-2018 Financial Services Agreement on 26 June 2015. They will, upon taking effect, supersede the 2013-2016 Business Services Agreement, the 2013-2016 Financial Services Agreement and the CEC Technology Financial Services Agreement, respectively. The services to be provided under the 2015-2018 Business Services Agreement are substantially the same as those prescribed in the 2013-2016 Business Services Agreement. Similarly, the terms under the 2015-2018 Financial Services Agreement are substantially the same as those prescribed in the 2013-2016 Financial Services Agreement and CEC Technology Financial Services Agreement.

### **2. 2015-2018 Business Services Agreement**

The 2015-2018 Business Services Agreement provides a framework between the Company and CEC under which the Company and any member of the CEC Group may enter into separate supplemental agreement(s) setting out the terms and conditions for the business services required from time to time. The 2015-2018 Business Services Agreement was entered into on a non-exclusive basis and does not create any obligations on the Group to enter into any agreement(s) with any member of the CEC Group for the business services. Any member of the CEC Group is one of a number of companies which the Group may enter into agreement(s) for the business services. The Group may enter into agreement(s) for the business services with any member of the CEC Group and/or other companies, as it sees fit.

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To assess the fairness and reasonableness of the terms of the 2015-2018 Business Services Agreement, we have considered the following:

***a. Terms of the 2015-2018 Business Services Agreement***

*Sourcing or purchase from the CEC Group*

We note that pursuant to the 2015-2018 Business Services Agreement:

- (i) All outsourcing and/or purchase transactions shall be undertaken on normal commercial terms or on terms no less favourable to the Enlarged Group than terms available to or from independent third parties. In particular, the transactions are to be carried out on a market oriented basis. Specifically, the Enlarged Group is neither obliged nor committed to outsource or exclusively purchase from the CEC Group in that the Enlarged Group is free to engage other third party service providers or suppliers should the Management deem that they offer more competitive prices for comparable quality of services and products.
- (ii) The service charges and purchase prices are to be determined after arm's length negotiation with reference to the pricing of the end products according to the customer order, the complexity of the particular work, the raw materials and technology involved and the market price, being (a) the prices at which same or comparable type of products or services provided by independent third parties in the same area in the ordinary and usual course of business; or, in the absence of which, (b) the prices at which same or comparable type of products or services provided by independent third parties in the ordinary and usual course of business. Please refer to the paragraph headed "Internal policy regarding the Continuing Connected Transactions" in this letter for our assessment on the Enlarged Group's relevant internal control policies. The consideration payable by the Enlarged Group under the agreement will be settled in cash according to the terms upon which the services are provided.

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In relation to the above, we have obtained samples from the Group and Huahong, and compared unit prices of past purchases and relevant service charges per unit for modules obtained from the CEC Group with those of similar products provided by independent third party service providers and noted that the prices per unit and service charges per unit to be no less favourable than terms with independent third parties. We have also compared the purchase prices of raw materials purchased from independent third party suppliers against those purchased from the CEC Group and found that the prices are no less favourable than terms with independent third parties. In order to select a representative sample throughout the three years ended 31 December 2014 and four months ended 30 April 2015, samples were selected from transactions for similar product/service types undertaken during each of the above period. Samples from the Group and Huahong for each of the three years ended 31 December 2014 include (i) top 5 transactions of each of the sale of products and the purchase of services; and (ii) an additional 5 randomly selected transactions of each of the sale of products and the purchase of services, whilst samples from the Group and Huahong for the four months ended 30 April 2015, on a pro-rata basis, include (i) top 3 transactions of each of the sale of products and the purchase of services; and (ii) an additional 2 randomly selected transactions of each of the sale of products and the purchase of services.

### *Sale of products to the CEC Group*

We note that pursuant to the 2015-2018 Business Services Agreement:

- (i) The sales transactions shall be undertaken on normal commercial terms or on terms no less favourable to the Enlarged Group than terms available to or from independent third parties. In particular, the Enlarged Group is neither obliged nor committed to sell only to the CEC Group if the terms offered are commercially unreasonable (e.g. price is not comparable to prevailing market prices) and the Enlarged Group is free to sell its products to other third party customers at comparable or higher selling prices where appropriate.
- (ii) Price of products will be determined based on arm's length negotiation with reference to the Enlarged Group's assessment of the general market price of that type of product which in turn takes into account the previous transactions with other customers who are independent third parties of the Enlarged Group in respect of similar products within six months and any market information based on the experience of the

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Management, the dealings with other players in the market and industry level profit margin available at that time. The consideration receivable by the Enlarged Group under the agreements will be settled in cash according to the terms upon which the products are provided.

With regards to the above, we have reviewed samples of historical terms and sale price of products for transactions between the CEC Group and the Group as well as those between Huahong and the CEC Group, and found that they are consistent with the price determination basis as mentioned above. Sale price per unit of products sold by the Group/Huahong to the CEC Group have also been compared to sale prices per unit of similar products sold to respective independent third party customers and were found to be no less favourable than terms with independent third parties. In order to select representative samples throughout the three years ended 31 December 2014 and four months ended 30 April 2015, samples were selected from transactions undertaken during each of the above period.

Taking into account the above factors, we consider the transactions contemplated under the 2015-2018 Business Services Agreement to be on normal commercial terms and are fair and reasonable so far as the Independent Shareholders are concerned.

***b. Reasons for and benefits of the 2015-2018 Business Services Agreement***

Following the completion of the Huada Semiconductor Acquisition, Huahong will become an indirect non wholly-owned subsidiary of the Company. Huahong has on-going transactions with the CEC Group which are similar to those contemplated under the 2013-2016 Business Services Agreement in its ordinary and usual course of business. These transactions will, after the completion of the Huada Semiconductor Acquisition, become continuing connected transactions of the Company. In order to streamline the continuing connected transactions between members of the Group (including Huahong after the completion of the Huada Semiconductor Acquisition) and members of the CEC Group, the Company entered into the 2015-2018 Business Services Agreement with CEC which will, upon taking effect, supersede the 2013-2016 Business Services Agreement.

It is our understanding from the Management that the Group's processing, testing and assembling procedures on integrated circuit products are outsourced to specialised service providers, including the CEC Group and that a majority of the

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Group's products are for specific application. As such, the raw materials and modules employed by the Group are usually product-specific and may vary largely depending on the customers' requirement.

According to the Management, the CEC Group has continued to be efficient in fulfilling the outsourcing and purchase requirements of the Group and the close relationship of the Group and CEC Group has thus far enabled the Group to better monitor the quality of the services and materials supplied. Moreover, the services provided by the CEC Group have been maintained at high standard and supply of raw materials and modules has been reliable and at competitive prices throughout the tenure of previous business services agreement. As such, the Management is of the view that it is commercially reasonable to continue such business relationship with CEC Group, which is an important supplier for the Group.

Regarding the sales transactions, CEC Group has a longstanding business relationship with the Group whereby CEC Group purchases products such as integrated circuit cards and smart cards modules and chips from the Group. We note from the Company's annual reports that sales to the CEC Group represented approximately 7.0% and 12.7% of the Group's revenue in the two years ended 31 December 2013 and 2014 respectively. Furthermore, according to the Management, the Group has a good record in collecting trade receivables from the CEC Group and has not encountered any significant disputes or problems related thereto in the past.

In light of the above, we concur with the Directors that the transactions contemplated under the 2015-2018 Business Services Agreement are vital and integral to the Enlarged Group's business operations. Together with the fact that (i) the transactions contemplated under the 2015-2018 Business Services Agreement will continue to be conducted on normal commercial terms or on terms no less favourable to the Enlarged Group than terms available to and from independent third parties (further elaborated above); and (ii) the transactions contemplated under the 2015-2018 Business Services Agreement are undertaken in the ordinary and usual course of the Enlarged Group's business given the respective principal business of the Group, Huahong and the CEC Group, we concur with the Directors that the entering of the 2015-2018 Business Services Agreement is in the interests of the Company and the Shareholders as a whole.

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**c. Proposed caps for the 2015-2018 Business Services Agreement**

*(i) Historical financial information and trading prospects*

Below is a table setting out the Group's (i) revenue; (ii) cost of sales; (iii) sales to the CEC Group; and (iv) outsourcing and/or purchases from the CEC Group for the two years ended 31 December 2013 and 2014 as extracted from the Company's respective published annual reports.

|                                                                                                      | <b>For the year ended 31<br/>December</b> |                 |
|------------------------------------------------------------------------------------------------------|-------------------------------------------|-----------------|
|                                                                                                      | <b>2013</b>                               | <b>2014</b>     |
|                                                                                                      | <i>HK\$'000</i>                           | <i>HK\$'000</i> |
| Revenue                                                                                              | 1,321,606                                 | 1,357,062       |
| Sales of products to<br>the CEC Group                                                                | 92,950                                    | 172,652         |
| Percentage of revenue                                                                                | 7.0%                                      | 12.7%           |
| Cost of sales                                                                                        | 728,677                                   | 773,767         |
| Products processing, testing and assembling<br>services and purchase of raw materials and<br>modules | 451,708                                   | 471,949         |
| Percentage of cost of sales                                                                          | 62.0%                                     | 61.0%           |

*Source: Company's 2013 and 2014 annual reports*

As shown in the table above, sale of products to the CEC Group represented approximately 7.0% and 12.7% of the Group's total revenue for the year ended 31 December 2013 and 2014 respectively, while outsourcing/purchases from the CEC Group remained stable, representing approximately 62.0% and 61.0% of the Group's cost of sales for the same period respectively. It was noted that whilst there was an increase of approximately 2.7% in the Group's total revenue from 2013 to 2014, sales to the CEC Group increased significantly by approximately 85.7% in the same period.

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We understand from the Management that such variation between the transactions with the CEC Group and the Group's overall business trends were mainly attributable to the market oriented approach adopted by the Group in that the Group opts to purchase and/or sell to parties offering the most favourable terms. Further, as aforementioned, a majority of the Group's products are for specific applications and the production process requires raw materials and modules with different specifications. The Group does not rely solely on the CEC Group to supply all or majority of products or services, except in the circumstances when the Group already have agreements with customers for the usage of certain products or services specifically provided by the CEC Group and applied in the products designed by the Group, then the Group must purchase such products or services from the CEC Group. If the Group were to switch to another supplier, the Group will have to re-open the negotiation with the customers, and under the current competitive environment, the likelihood to maintain the price, the quantity, the profit margin and/or to secure the contract may be at risk, which in turn, may not be in the interest of the Company. Hence, the Enlarged Group may not be able to easily switch to other supplier in such circumstances. In view of the above, it is not practical to impose a limit on the amount of such purchases of products or services from the CEC Group; but for managing the potential operational risk associated with this type of reliance on the CEC Group, there is already an annual cap for the total amount of purchase of products and services to be made by the Group from the CEC Group and the relevant internal control measures put in place as described in the paragraph headed "4. Internal policy regarding the continuing connected transactions" below. In addition, the ratio of consideration payable by the Group for each of the year ended 31 December 2012, 2013 and 2014 and the six months ended 30 June 2015 was approximately 83.1%, 62.0%, 61.0% and 45.7% respectively, and the reliance of the CEC Group was on a reducing trend. Considering the CEC Group has historically proven to be an efficient and reliable supplier to the Group, it is therefore commercially reasonable to continue outsourcing/purchasing from the CEC Group. In view of the above, we are of the view that the transactions contemplated under the 2015-2018 Business Services Agreement will be conducted in the Group's ordinary and usual course of business. Detailed discussion on the fairness and reasonableness of the transactions is set out in paragraph headed "Reasons for and benefits of the 2015-2018 Business Services Agreement" above.

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We note that Huahong's sales to the CEC Group represented approximately 7.1% and 7.8% of its total revenue for the year ended 31 December 2013 and 2014 respectively, whilst outsourcing/purchases from the CEC Group represented approximately 8.9% and 26.2% of Huahong's cost of sales for the same period respectively. It was noted that Huahong's total sales and total cost of sales decreased by approximately 4.6% and 0.8% from 2013 to 2014 respectively, whilst its sales to the CEC Group decreased by approximately 8.6% and outsourcing/purchasing from the CEC Group increased significantly by approximately 191.0% in the same period.

We understand from the Management that Huahong also adopts the market oriented approach and opts to purchase and/or sell to parties offering the most favourable terms, as such there was variation between the transactions with the CEC Group and Huahong's overall business trends.

*(ii) Existing caps and historical variances*

Below is a table setting out (aa) each category of continuing connected transactions contemplated under the 2013-2016 Business Services Agreement; (bb) the existing cap approved for the 2013-2016 Business Services Agreement; (cc) the historical amount of charges recorded for each of the year ended 31 December 2012, 2013 and 2014 and the four months ended 30 April 2015; and (dd) the proposed cap for the 2015-2018 Business Services Agreement.

| Types of transaction                                                                                                | Existing caps/historical amount recorded |         |         | For the               |
|---------------------------------------------------------------------------------------------------------------------|------------------------------------------|---------|---------|-----------------------|
|                                                                                                                     |                                          |         |         | four months           |
|                                                                                                                     |                                          |         |         | ended                 |
|                                                                                                                     |                                          |         |         | 30 April              |
|                                                                                                                     | For the year ended 31 December           |         |         | 2015                  |
|                                                                                                                     | 2012                                     | 2013    | 2014    |                       |
|                                                                                                                     | RMB'000                                  | RMB'000 | RMB'000 | RMB'000               |
| Products processing, testing and assembling services and purchase of raw materials, modules, software and equipment |                                          |         |         |                       |
| Approved cap                                                                                                        | 770,000                                  | 656,000 | 852,000 | 1,064,000<br>(Note 1) |
| Historical amount paid/payable by the Group                                                                         | 475,977                                  | 360,445 | 373,949 | 98,094<br>(Note 2)    |
| Utilisation percentage                                                                                              | 61.8%                                    | 54.9%   | 43.9%   | 27.7%<br>(Note 3)     |
| Historical amount paid/payable by Huahong (Note 4)                                                                  | 41,939                                   | 29,728  | 86,501  | 8,569<br>(Note 2)     |

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| Types of transaction                                              | Existing caps/historical amount recorded |         |         | For the     |
|-------------------------------------------------------------------|------------------------------------------|---------|---------|-------------|
|                                                                   | For the year ended 31 December           |         |         | four months |
|                                                                   | 2012                                     | 2013    | 2014    | ended       |
|                                                                   | RMB'000                                  | RMB'000 | RMB'000 | 30 April    |
|                                                                   |                                          |         |         | 2015        |
|                                                                   |                                          |         |         | RMB'000     |
| <b>Sale of products</b>                                           |                                          |         |         |             |
| Approved Cap                                                      | 106,000                                  | 116,000 | 150,000 | 188,000     |
|                                                                   |                                          |         |         | (Note 1)    |
| Historical amount received/<br>receivable by the Group            | 82,258                                   | 74,170  | 136,730 | 46,600      |
|                                                                   |                                          |         |         | (Note 2)    |
| Utilisation percentage                                            | 77.6%                                    | 63.9%   | 91.2%   | 74.4%       |
|                                                                   |                                          |         |         | (Note 3)    |
| Historical amount received/<br>receivable by the Huahong (Note 4) | 51,730                                   | 34,083  | 35,452  | 7,078       |
|                                                                   |                                          |         |         | (Note 2)    |

*Notes:*

1. The amount refers to the annual cap for the year ending 31 December 2015.
2. The amount refers to the historical amount for the four months ended 30 April 2015, being the latest practicable date to ascertain such information prior to the despatch of the Circular.
3. The utilisation percentage has been annualised for illustration purpose only.
4. Huahong's historical transaction amounts are set out herein for reference as these are taken into consideration when determining the respective proposed caps under the 2015-2018 Business Services Agreement. Detailed analysis of which is set out in the following section.

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As shown in the table above, the Group utilised approximately 61.8%, 54.9% and 43.9% of the approved caps for the outsourcing and purchase transactions with the CEC Group (i.e. the historical transaction amounts payable by the Group) for the three years ended 31 December 2012, 2013 and 2014 respectively. For the four months ended 30 April 2015, the amount recorded for the outsourcing and purchase transactions with the CEC Group was approximately RMB98.1 million. When annualised for illustration purpose, the Group utilised approximately 27.7% of the approved cap for the four months ended 30 April 2015. It is noted that the utilisation had declined in the past year, which we understand from the Management was due to the fluctuations in demand for different products during certain periods which could be temporary. In any event, the transactions had been carried out on a market oriented basis and during those periods the prices of independent third parties had been more competitive than the CEC Group resulting in the lower utilisation.

In relation to the sale of products, the Group utilised approximately 77.6%, 63.9% and 91.2% of the approved caps for the amount of sales to the CEC Group (i.e. historical transaction amounts receivable by the Group) for the three years ended 31 December 2012, 2013 and 2014 respectively. For the four months ended 30 April 2015, the amount of sales to the CEC Group was approximately RMB46.6 million, representing an annualised utilisation rate of approximately 74.4%.

*(iii) Proposed caps*

| Types of transaction                                                                                                         | Proposed caps                                                                                                                                         |                                    |                |                                 |
|------------------------------------------------------------------------------------------------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------|------------------------------------|----------------|---------------------------------|
|                                                                                                                              | For the period<br>commencing<br>from the<br>completion of<br>the Huada<br>Semiconductor<br>Acquisition until<br>31 December<br>2015<br><i>RMB'000</i> | For the year ending<br>31 December |                | For the<br>six months<br>ending |
|                                                                                                                              |                                                                                                                                                       | 2016                               | 2017           | ending                          |
|                                                                                                                              |                                                                                                                                                       | 31 December                        | 31 December    | 30 June                         |
|                                                                                                                              |                                                                                                                                                       | 2018                               | 2018           | 2018                            |
|                                                                                                                              | <i>RMB'000</i>                                                                                                                                        | <i>RMB'000</i>                     | <i>RMB'000</i> | <i>RMB'000</i>                  |
| Products processing, testing and<br>assembling services and purchase<br>of raw materials, modules,<br>software and equipment |                                                                                                                                                       |                                    |                |                                 |
| Proposed cap                                                                                                                 | 300,000                                                                                                                                               | 780,000                            | 1,000,000      | 650,000                         |
| Sale of products                                                                                                             |                                                                                                                                                       |                                    |                |                                 |
| Proposed cap                                                                                                                 | 110,000                                                                                                                                               | 290,000                            | 370,000        | 240,000                         |

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### *Outsourcing and purchase*

We note that each of the proposed caps for the outsourcing and purchase of supplies have been determined with the reference to (i) the historical service fees from the CEC Group; (ii) the historical demand for raw materials, modules, software and equipment of the Group; (iii) expected demand and production plan of the Enlarged Group; and (iv) the costs of such services, raw materials, modules, software and equipment.

Moreover, since Huahong also undertakes transactions of similar nature with the CEC Group, Huahong's historical amounts (which are set out in the table under the paragraph headed "Existing caps and historical variances" in the previous section) were also taken into account when determining the proposed caps. In addition to this, we understand that the Management has also factored in the anticipated increase in demand for the products of the Group and Huahong arising from (i) the PRC's mobile telecommunications sector's transfer from 3G to 4G; and (ii) PBOC's intention to replace magnetic stripe cards with integrated circuit cards. Based on our own research<sup>1</sup>, given that 2014 was the first full year of 4G commercialisation for major telecom companies in the PRC, we note the number of existing 3G/4G subscribers representing approximately 63.9% and 11.2% of the total mobile subscribers of each of the two major telecom companies in the PRC in 2014 and such companies will continue to accelerate their customer migration from 2G and 3G network to 4G network in the near term so as to seize the opportunities arising from the 4G developments. During the six months ended 30 June 2015, it is noted that (i) the number of existing 3G/4G subscribers of one of the major telecom company mentioned above already reached approximately 68% (31 December 2014: 63.9%) of its total number of customers, of which the net addition of 4G customers was 22 million, reaching a total of approximately 29 million 4G customers; and (ii) the 4G customer base of the other major telecom company reached approximately 23% of its total number of customers (representing an increase of over 100% than the 11.2% recorded in 2014 mentioned above). In view of the foregoing, the proposed cap for the period commencing from the completion of the Huada Semiconductor Acquisition until 31 December 2015 were determined on an assumed increase of approximately 30% from the historical transaction amounts for the year ended 31 December 2014 and the purchase orders already received by the Group during the first half of 2015. Meanwhile, the respective proposed caps for the years ending 31 December 2016 and 2017 and the six months ending 30 June 2018 were determined on a

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<sup>1</sup> Information were gathered from the respective 2014 annual reports and 2015 interim reports of China Telecom Corporation Limited (stock code 728) and China Mobile Limited (stock code 941).

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year-on-year increase of approximately 30%, 28% and 30% respectively. On the bases described above, in particular, as the rate of increase in 4G customers from 2014 to the first half of 2015 was over 100%, the trend to switch to 4G is not expected to slow down when the major telecom companies in the PRC are continuing to invest and expand the 4G market, the potential to be derived from the new issuance of integrated circuit chip bankcards is expected to be significant and as also mentioned in the “Letter from the Board”, according to statistics published by the China Semiconductor Industry Association, the total revenue generated by the integrated circuit industry in PRC in 2014 increased 20.2% as compared to 2013 and the total revenue generated from the design of integrated circuits, one of the key stages in the supply chain, also increased 29.5% in 2014 as compared to 2013, we therefore believe the incremental increase of approximately 30% over each period mentioned above is reasonable.

In this regard, we note that such expectation is in line with the market. In particular, as discussed in the paragraph headed “1.7 Prospects of Huahong” above, growth in the integrated circuit industry is expected to be driven by the 4G mobile market, the rapid development of the Internet of Things sector and the replacement of magnetic stripe bankcards with those embedded with integrated circuit chips. In particular, given the growth of 4G terminals have outstripped expectation, the MIIT expects there will be intense competition in this segment, which will in turn lead to excess demand over supply for integrated chips embedded in SIM cards. In this connection the MIIT are of the view that domestic integrated circuit chips enterprises will be able to capture part of the market share. With regards to PBOC’s intention of replacing magnetic stripe bankcards with those embedded with integrated circuit chips, we note from 2015 onwards, PBOC has required the cessation of issuance of magnetic strip bankcards and that it is expected the number of new issuances of integrated circuit chip bankcards per year may reach several hundred million in the next few years.

It is our understanding that the average prices based on historical data of comparable products were adopted in deriving the respective proposed caps. While market price competition has been intensifying, the Management believes and we concur that prices of new products at any material time can better withstand price pressure to off-set the decrease in the prices of older products. Hence, we are of the view that by using the average historical prices of comparable products to determine the proposed caps is reasonable. In this regard, we have reviewed sample of transactions between the Group and the

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CEC Group as well as Huahong and the CEC Group and established that the unit prices from our sample are no less favourable than terms with independent third parties to those adopted in deriving the respective proposed caps.

### *Sales of products*

In respect of the respective proposed caps of the sales transactions to the CEC Group, we note that the Management has made reference to (i) historical sales; (ii) the expected demand of the Enlarged Group's products by the CEC Group; and (iii) the order status of the products.

In this regard, we note that the Group's historical sales transactions maintained at high levels of utilisation rates for the three years ended 31 December 2014 and four months ended 30 April 2015. The projected growth in proposed cap is due to the expected growth in sales volume which is in line with the Enlarged Group's business strategy to expand the market share of its products set out in the Company's annual report for the year ended 31 December 2014 as well as the abovementioned future prospects of the Group and Huahong. Furthermore, given that Huahong is also engaged in similar business as the Group and has continuous sales transactions with CEC Group, upon completion of the Huada Semiconductor Acquisition, such sales transactions are also expected to increase.

Similar to the outsourcing and purchases transactions, the respective proposed caps for sales transactions were derived by adopting the historical average unit prices of comparable products. In this regards, we have reviewed samples of the Group's and Huahong's respective transactions with the CEC Group and established that the unit prices represented in our sample are no less favourable than terms with independent third parties to those adopted in deriving the respective proposed caps.

When arriving at the above caps, the Directors have considered the fact that while market price competition has been intensifying, prices of new products (such as those relating to transfer from 3G to 4G) can better withstand price pressures. Taking into account (i) the historical low utilisation rate of the annual caps for the purchases of products or services from the CEC Group, the Group includes certain buffer to the proposed caps for such purchases to cater for the fluctuation in demand for certain products during the period ending 30 June 2018; and (ii) the above factors and reasons, we are of the view that the respective proposed caps with regard to the transactions contemplated under the 2015-2018 Business Services Agreement for the

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period commencing from the completion of the Huada Semiconductor Acquisition until 31 December 2015, for each of the year ending 31 December 2016 and 2017 and the six months ending 30 June 2018 are fair and reasonable.

### **3. The 2015-2018 Financial Services Agreement**

The 2015-2018 Financial Services Agreement provides a framework between the Company and CEC Finance under which any member of the Group and CEC Finance may enter into separate supplemental agreement(s) setting out the terms and conditions for various financial services required from time to time. The interest rates offered by CEC Finance under the 2015-2018 Financial Services Agreement are subject to negotiations between the parties.

To assess the fairness and reasonableness of the terms of the 2015-2018 Financial Services Agreement, we have considered the following:

#### ***a. Terms of the 2015-2018 Financial Services Agreement***

We note that pursuant to the 2015-2018 Financial Services Agreement:

- (i) All transactions contemplated under the 2015-2018 Financial Services Agreement shall be undertaken on normal commercial terms or on terms no less favourable to the Group than terms available from other domestic commercial banks or financial institutions.
- (ii) The 2015-2018 Financial Services Agreement does not create any obligation on the part of the Enlarged Group to utilise any particular services of CEC Finance. Other than time deposits which have specified deposit terms, the Enlarged Group may at any time withdraw the funds deposited with CEC Finance without incurring any penalty. The Enlarged Group may obtain financial services available from CEC Finance, and/or any other financial institutions as it sees fit.
- (iii) Interest rates on deposits and financial assistance offered by CEC Finance to the Enlarged Group will be determined with reference to, and shall not be less than, the rates offered to the Enlarged Group by other domestic commercial banks for comparable deposits or financial assistance.

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- (iv) The fees and commissions for the fee-based and commission-based financial services provided by CEC Finance to the Enlarged Group will be determined with reference to and shall not be higher than those charged by other domestic commercial banks or financial institutions for the same type of financial services. In particular, where available, the Enlarged Group will refer to standard or reference rates promulgated by the PBOC prior to agreeing with CEC Finance on the pricing of the relevant financial services.
- (v) The Enlarged Group will be able to obtain unsecured RMB and foreign currencies loans from CEC Finance, which according to the Management, is considered to be a more favourable arrangement than those offered by domestic commercial banks and financial institutions.

For the deposit services, we have obtained samples of the Group and Huahong and compared the interest rates on deposits of various terms offered by CEC Finance with the standard or reference rates promulgated by the PBOC and found the rates to be comparable. Regarding the provision of financial assistance to the Group, rates offered by CEC Finance were also comparable to those promulgated by the PBOC. As for fee-based and commission-based financial services, we have reviewed samples of previous transactions and found the fees and commissions charged to the Group to be no less favourable than terms with independent third parties or comparable to the standard or reference rates promulgated by the PBOC. In order to select a representative sample throughout the three years ended 31 December 2014 and four months ended 30 April 2015, samples were selected from transactions undertaken during each of the above period.

Taking into account the aforesaid factors, we consider the transactions contemplated under the 2015-2018 Financial Services Agreement to be on normal commercial terms and are fair and reasonable so far as the Independent Shareholders are concerned.

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***b. Reasons for and benefits of the 2015-2018 Financial Services Agreement***

Following the completion of the Huada Semiconductor Acquisition, Huahong will become an indirect subsidiary of the Company. Huahong has on-going transactions with the CEC Group which are similar to those contemplated under the 2013 Financial Services Agreement in its ordinary and usual course of business. These transactions will, after the completion of the Huada Semiconductor Acquisition, become continuing connected transactions of the Company. In order to streamline the continuing connected transactions among members of the Group (including Huahong after the completion of the Huada Semiconductor Acquisition) and members of the CEC Group, the Company entered into the 2015-2018 Financial Services Agreement with CEC Finance which will, upon taking effect, supersede the 2013 Financial Services Agreement.

As evidenced by historical transactions, CEC Finance has been providing various financial services to the Group and Huahong in the past. From our discussion with the Management, we note that this longstanding relationship has enabled CEC Finance to have a better understanding of the operations of the Enlarged Group which in turn leads to expedient and efficient delivery of such services. Moreover, it is commercially reasonable and beneficial to continue with such arrangement since it will maintain stability in the financial operation of the Enlarged Group.

We also note that as a regulated financial institution, CEC Finance is required to comply with all rules and operations requirements of the regulatory authorities, namely the PBOC and the CBRC. As such, the continued utilisation of the financial services provided by CEC Finance will not expose the Enlarged Group to additional financial risk as compared to the Enlarged Group utilising comparable services provided by similar financial institutions that are governed by the same rule and operational requirements of the PBOC and the CBRC. Further, the various financial services provided by CEC Finance under the 2015-2018 Financial Services Agreement will continue to provide the Enlarged Group with the right and flexibility to secure additional source of financing and services at reasonable cost as and when necessary.

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In view of the above and that (i) the transactions contemplated under the 2015-2018 Financial Services Agreement will continue to be conducted on normal commercial terms or on terms no less favourable to the Group than terms available from other domestic commercial banks and financial institutions; and (ii) the transactions contemplated under the 2015-2018 Financial Services Agreement are undertaken in the ordinary and usual course of the Enlarged Group's business given the principal businesses of CEC Finance, we concur with the Director's that the entering of the 2015-2018 Financial Services Agreement is in the interests of the Company and the Shareholders as a whole.

**c. Proposed caps for the 2015-2018 Financial Services Agreement**

*(i) Existing caps and historical variances*

Below is a table setting out (aa) each category of continuing connected transactions contemplated under the 2013-2016 Financial Services Agreement; (bb) the existing cap approved for the 2013-2016 Financial Services Agreement; (cc) the historical amount recorded for each of the year ended 31 December 2012, 2013 and 2014 and the four months ended 30 April 2015; and (dd) the proposed cap for the 2015-2018 Financial Services Agreement.

| Type of transaction                                                                          | Existing caps/historical amount recorded |         |                     |                     |
|----------------------------------------------------------------------------------------------|------------------------------------------|---------|---------------------|---------------------|
|                                                                                              | For the year ended 31 December           |         |                     |                     |
|                                                                                              | 2012                                     | 2013    | 2014                | 2015                |
|                                                                                              | RMB'000                                  | RMB'000 | RMB'000             | RMB'000             |
| <b>Provision of deposit services</b>                                                         |                                          |         |                     |                     |
| Approved cap                                                                                 | 80,000                                   | 680,000 | 680,000             | 480,000             |
| Historical maximum daily balance of deposits maintained by the Group with CEC Finance        | 80,000                                   | 276,000 | 398,351<br>(Note 1) | 383,581<br>(Note 2) |
| Utilisation percentage                                                                       | 100.0%                                   | 40.6%   | 58.6%               | 79.9%               |
| Historical maximum daily balance of deposits maintained by Huahong with CEC Finance (Note 3) | 410,374                                  | 350,385 | 307,050             | 95,229              |

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| Type of transaction                                                                                                                                                           | Existing caps/historical amount recorded<br>For the year ended 31 December |                |                            |                           |
|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|----------------------------------------------------------------------------|----------------|----------------------------|---------------------------|
|                                                                                                                                                                               | 2012                                                                       | 2013           | 2014                       | 2015                      |
|                                                                                                                                                                               | <i>RMB'000</i>                                                             | <i>RMB'000</i> | <i>RMB'000</i>             | <i>RMB'000</i>            |
| <b>Provision of financial assistance</b>                                                                                                                                      |                                                                            |                |                            |                           |
| Approved cap                                                                                                                                                                  | 80,000                                                                     | 680,000        | 680,000                    | 480,000                   |
| Historical maximum daily balance of financial assistance provided by CEC Finance to the Group                                                                                 | –                                                                          | –              | 361,000<br><i>(Note 1)</i> | 50,000<br><i>(Note 2)</i> |
| Utilisation percentage                                                                                                                                                        | 0%                                                                         | 0%             | 53.1%                      | 10.4%                     |
| Historical maximum daily balance of financial assistance provided by CEC Finance to Huahong <i>(Note 3)</i>                                                                   | –                                                                          | –              | –                          | –                         |
| <b>Provision of fee-based and commission-based financial services</b>                                                                                                         |                                                                            |                |                            |                           |
| Approved cap                                                                                                                                                                  | 4,000                                                                      | 10,750         | 10,750                     | 10,750                    |
| Historical amount of fees and commissions payable by the Group to CEC Finance for the fee-based and commission-based financial services provided by CEC Finance               | –                                                                          | –              | 445<br><i>(Note 1)</i>     | 28<br><i>(Note 2)</i>     |
| Utilisation percentage                                                                                                                                                        | 0%                                                                         | 0%             | 4.1%                       | 0.8%<br><i>(Note 4)</i>   |
| Historical amount of fees and commissions payable by Huahong to CEC Finance for the fee-based and commission-based financial services provided by CEC Finance <i>(Note 3)</i> | 31                                                                         | 22             | 16                         | –                         |

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*Notes:*

1. CEC Technology became a wholly-owned subsidiary of the Company following the completion of the acquisition of CEC Technology on 26 June 2014. The transactions between CEC Technology and its subsidiaries and the CEC Group have since then become continuing connected transactions of the Company.
2. The amount refers to historical amount for the four months ended 30 April 2015, being the latest practicable date to ascertain such information prior to the despatch of the Circular.
3. Huahong's historical transaction amounts are set out herein for reference as these are taken into consideration when determining the respective proposed caps under the 2015-2018 Financial Services Agreement. Detailed analysis of which is set out in the following paragraph headed "(ii) Proposed caps" below.
4. The utilisation percentage has been annualised for illustration purpose only.

As shown in the table above, the Group had utilised 100% and approximately 40.6% and 58.6% of the approved caps for the maximum daily balance of deposits maintained with CEC Finance during the three years ended 31 December 2012, 2013 and 2014 respectively. During the four months ended 30 April 2015, the maximum daily balance which had been maintained by the Group with CEC Finance was approximately RMB383.6 million, representing a utilisation rate of approximately 79.9%. We also note that the maximum daily balance of deposits maintained by Huahong with CEC Finance were substantial during the corresponding period. In relation to the financial assistance and fee-based and commission-based financial services provided by CEC Finance to the Group, the Group did not obtain any such services from CEC Finance during the two years ended 31 December 2012 and 2013. During the year ended 31 December 2014 and four months ended 30 April 2015, the maximum daily balance recorded for the financial assistance provided by CEC Finance to the Group were approximately RMB361.0 million and RMB50.0 million, representing a utilisation rate of approximately 53.1% and 10.4% respectively. For the amount of fee-based and commission-based financial services, the amounts payable by the Group to CEC Finance were approximately RMB445,000 and RMB28,000 for the year ended 31 December 2014 and four months ended 30 April 2015 respectively, representing a utilisation rate of approximately 4.1% and 0.8% (annualised) respectively.

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## LETTER FROM ALTUS CAPITAL

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(ii) *Proposed caps*

| Type of transaction                                                   | Proposed caps                                                                                                                       |                                    |                |                                                    |
|-----------------------------------------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------|------------------------------------|----------------|----------------------------------------------------|
|                                                                       | For the period<br>commencing<br>from the<br>completion<br>of the Huada<br>Semiconductor<br>Acquisition until<br>31 December<br>2015 | For the year ending<br>31 December |                | For the<br>six months<br>ending<br>30 June<br>2018 |
|                                                                       |                                                                                                                                     | 2016                               | 2017           |                                                    |
|                                                                       | <i>RMB'000</i>                                                                                                                      | <i>RMB'000</i>                     | <i>RMB'000</i> | <i>RMB'000</i>                                     |
|                                                                       |                                                                                                                                     |                                    |                |                                                    |
| <b>Provision of deposit services</b>                                  |                                                                                                                                     |                                    |                |                                                    |
| Proposed cap                                                          | 700,000                                                                                                                             | 740,000                            | 780,000        | 820,000                                            |
| <b>Provision of financial assistance</b>                              |                                                                                                                                     |                                    |                |                                                    |
| Proposed cap                                                          | 700,000                                                                                                                             | 740,000                            | 780,000        | 820,000                                            |
| <b>Provision of fee-based and commission-based financial services</b> |                                                                                                                                     |                                    |                |                                                    |
| Proposed cap                                                          | 5,000                                                                                                                               | 10,000                             | 10,000         | 5,000                                              |

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## LETTER FROM ALTUS CAPITAL

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### *Provision of deposit services and financial assistance*

When proposing the maximum daily balance of deposits maintained by the Group with CEC Finance, the Management has taken into consideration of the caps relating to the provision of financial assistance by CEC Finance to the Group. In particular, as part of its treasury policy, CEC, being the ultimate controlling shareholder of the Group, is prepared to provide financial assistance of the amounts as illustrated in the above table to the Group through CEC Finance. We understand that such proposed caps are the maximum amount of funds, the limit proposed by CEC Finance based on their internal assessment on the maximum amount of unsecured and secured financial assistance, which they may provide to the Enlarged Group. This is in turn determined with reference to the possible capital and operational needs of the Enlarged Group. We understand from the Management that in the case where the drawdown financial assistance provided by CEC Finance is not immediately deployed, such amount will be deposited with CEC Finance. As such, to facilitate such procedures, the proposed maximum daily balance of deposit services was set at the equivalent amount of the limit for the financial assistance that could be provided. We have discussed with the Management and understand that other domestic commercial banks and/or other financial institutions would usually request for a security in respect of financial assistance of such magnitude. Meanwhile, the financial assistance provided by CEC Finance will be on an unsecured basis.

Notwithstanding the relatively low utilisation of the historical caps for fee-based and commission-based financial services, we consider that it is commercially reasonable for the Group to maximise its financial flexibility (in particular during the periods when such services are to be used within short notice) by accepting the highest limit of financial assistance offered by CEC Finance. In view of the above and that the Group is neither obliged nor committed to carry out any transactions contemplated under the 2015-2018 Financial Services Agreement if the terms, interest rates on deposits and financial assistance are less favorable in comparison to those offered by other domestic commercial banks or financial institutions, we consider the aforementioned proposed caps to be reasonable.

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## LETTER FROM ALTUS CAPITAL

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### *Provision of fee-based and commission-based financial services*

Fees and commission payable by the Group to CEC Finance refers to the charges in relation to the provision of guarantee services, handling services, fund management, agency services and financial consultancy services to be provided by CEC Finance. When estimating the proposed caps for fee-based and commission-based financial services, the Group has in particular taken into account the amount of handling services to be provided by CEC Finance. In this respect, the Group intends to pledge its cash resources in Hong Kong in return for cash-backed facilities from CEC Finance which will be used by the Group to finance its operations in the PRC. CEC Finance will charge a handling fee for this service, which amount is estimated taking into account the Group's cash balances in Hong Kong multiply by the fee rate expected to be charged by CEC Finance based on prevailing market. The fees for other miscellaneous service are expected to be comparatively nominal.

Based on the above, we are of the view that the respective proposed caps under the 2015-2018 Financial Services Agreement for the period commencing from the completion of the Huada Semiconductor Acquisition until 31 December 2015, for each of the two years ending 31 December 2016 and 2017 and the six months period ending 30 June 2018 are fair and reasonable.

#### **4. Internal policy regarding the continuing connected transactions**

The Company has established internal control policy and procedure as a means to ensure transactions with the CEC Group are on normal commercial terms and in compliance with the relevant provisions in the Listing Rules.

It is noted that internal control measures for 2015–2018 Business Services Agreement conducted by the Group are as follows:

Before confirming the pricing of provision of products processing, testing and assembling services by the CEC Group, and purchase of raw materials, modules, software and equipment from the CEC Group, the Group will refer to two other contemporaneous

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## LETTER FROM ALTUS CAPITAL

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transactions with the independent third parties in similar quantities to determine if the prices and terms offered by the CEC Group are fair, reasonable and no less favorable than those offered by independent third parties, or the pricing of the end products according to the customer's order, the complexity of the particular work and the raw materials and technology involved. Before confirming the pricing of sale of products to the CEC Group, the Group will refer to previous transactions with independent third parties in respect of similar products and similar quantities within 6 months and any market information based on the experience of the Group's management, the dealings with other players in the market, and industry level profit margin, which may be available at that time, and make an assessment of the general market price of that type of product. In particular, we note that the pricing of the transactions under the 2015-2018 Business Services Agreement are subject to an internal approval process whereby the purchasing/sales department (as the case maybe) is required to obtain approval from the legal department and the finance department prior to confirming the prices. For transactions exceeding RMB5 million, approval from any one director of the relevant member of the Group is required. For details, please refer to the paragraph headed "(ii) Sale of products to the CEC Group" in the "Letter from the Board" of the Circular.

With regards to the transactions under the 2015-2018 Financial Services Agreement, the Enlarged Group will obtain interest rates and/or fee/commission (as appropriate) offered by one or two reputable domestic commercial banks or financial institutions with whom the Enlarged Group has established business relationships to compare those offered by CEC Finance.

It is noted that internal control measures for 2015-2018 Financial Services Agreement conducted by the Group are as follows:

Before making a deposit with, seeking financial assistance from or using fee-based and commission-based financial services from CEC Finance, the Group would obtain the interest rates and/or fees/commissions (as appropriate) offered by one or two reputable domestic commercial banks or financial institutions which the Group has established business relationship and compare that with the interest rates and/or fees/commissions offered by CEC Finance. In respect of any deposit services or financial assistance provided by CEC Finance to the Group, an internal application is submitted to the finance departments of the relevant member of the Group procuring such services for approval. For transactions exceeding RMB100 million, the interest rates are subject to further approval by any one Director.

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## LETTER FROM ALTUS CAPITAL

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We also noted that from the Company's annual reports that the independent non-executive Directors had reviewed the Group's continuing connected transactions annually and had confirmed in the Company's annual report that the transactions thereunder have been (i) in the ordinary and usual course of business of the Group; (ii) on normal commercial terms; and (iii) in accordance with the relevant agreements governing them on terms that are fair and reasonable and in the interests of the Company and the Shareholders as a whole. In this regard, we are of the view that the transactions contemplated under the 2015-2018 Business Services Agreement and 2015-2018 Financial Services Agreement will be carried out on normal commercial terms and at terms no less favourable to the Company than those offered to/from independent third party.

In addition, we also noted that the Company has engaged PricewaterhouseCoopers ("PwC"), the Company's auditor, to report to the Board on the Group's continuing connected transactions. In accordance with Rule 14A.56 of the Listing Rules that in each of the two years ended 31 December 2013 and 2014, the Company's auditor has confirmed that nothing has come to their attention that causes them to believe that (i) the disclosed transactions have not been approved by the Board; (ii) the transactions were not, in all material respects, in accordance with the pricing policies of the Group; (iii) the transactions were not entered into, in all material respects, in accordance with the relevant agreements governing such transactions; and (iv) the transactions have exceeded their respective maximum aggregate annual value as disclosed in the previous announcements of the Company.

Given the above, we consider that there exist appropriate procedures and arrangements to ensure that the transactions contemplated under the 2015-2018 Business Services Agreement and the 2015-2018 Financial Services Agreement will be conducted on terms in compliance with the provisions of the Listing Rules.

### RECOMMENDATIONS

#### 1. The Shanghai Huahong Acquisition

Having considered the above principal factors and reasons, we are of the view that the (i) Shanghai Huahong Acquisition is in the interests of the Company and the Shareholders as a whole despite that the Shanghai Huahong Acquisition was not in the ordinary and usual course of business of the Group; and (ii) the terms of the Shanghai Huahong Acquisition Agreements and the transactions contemplated thereunder are on normal commercial terms and are fair and reasonable so far as the Independent Shareholders are concerned. Accordingly, we recommend the Independent Shareholders, as well as the Independent Board Committee to advise the Independent Shareholders, to vote in favour of the resolution(s) to be proposed at the SGM to approve the Shanghai Huahong Acquisition Agreements and the transactions contemplated thereunder at the SGM.

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## LETTER FROM ALTUS CAPITAL

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### 2. Continuing Connected Transactions

Having considered the above principal factors and reasons, we are of the view as at the date hereof that (i) the transactions contemplated under the 2015-2018 Business Services Agreement and the 2015-2018 Financial Services Agreement are in the Group's ordinary and usual course of business and the respective proposed caps related thereto are in the interests of the Company and the Shareholders as a whole; (ii) the terms of the aforesaid agreements are on normal commercial terms and are fair and reasonable so far as the Independent Shareholders are concerned; and (iii) the respective proposed caps have been fairly and reasonably arrived at. Accordingly, we would advise the Independent Shareholders, as well as the Independent Board Committee to recommend the Independent Shareholders, to vote in favour of the ordinary resolutions approving the 2015-2018 Business Services Agreement, the 2015-2018 Financial Services Agreement and the respective proposed caps related thereto to be proposed at the SGM.

Yours faithfully,  
For and on behalf of  
**Altus Capital Limited**  
**Chang Sean Pey**  
*Executive Director*

*Mr. Chang Sean Pey ("Mr. Chang") is a Responsible Officer of Altus Capital Limited licensed to carry out Type 4 (advising on securities), Type 6 (advising on corporate finance) and Type 9 (asset management) regulated activities under the SFO and permitted to undertake work as a sponsor. He is also a Responsible Officer of Altus Investments Limited licensed to carry out Type 1 (dealing in securities) regulated activity under the SFO. Mr. Chang has over 15 years of experience in banking, corporate finance and advisory and investment management. In particular, he has participated in sponsorship work for initial public offerings and acted as financial adviser or independent financial adviser in various corporate finance advisory transactions.*

*With the exception of the transaction involving an acquisition of a property transfer right by Huada Electronics from a connected person as described in the circular of the Company dated 20 December 2013, Altus Capital Limited has not acted as an independent financial adviser of the Company's other transactions in the last two years from the date of the Circular. Pursuant to Rule 13.84 of the Listing Rules, and given that remuneration for our engagement to opine on this is at a market level and is not conditional upon successful passing of the resolutions and that our engagement is on normal commercial terms, Altus Capital Limited is independent of the Company.*

**MANAGEMENT DISCUSSION AND ANALYSIS OF HUAHONG**

The following discussion and analysis should be read in conjunction with the financial information of Huahong for the three years ended 31 December 2014 and the four months ended 30 April 2015, as set out in Appendix III to this circular.

**Business and financial overview**

Huahong is an industrial leader in the design of the integrated circuit sector in the PRC. It has a comprehensive domestic smart card product line, with technology focusing on the design and system development of contact, contactless and dual-interface integrated circuit chips, which are widely used in sectors such as social security (social security cards), telecommunications (SIM cards), public transport (public transport cards), identity authentication (identity cards and residence permits), electronic travel documents (electronic passports) and financial security (bank cards). Huahong also focuses on providing customers with system solutions to address their business and operational challenges. In recent years, Huahong launched a series of solutions including the public transport one-card pass solution, residence permit solution, Shanghai World Expo ticketing solution, commercial encryption access control system solution, and multi-applications financial solution. These solutions embrace the technical elements of application software, key management system and encrypted integrated circuit chips to form the application-oriented and customer-oriented solutions that enhance the efficiency and security of supply chains, transactions and the authentication of goods and people.

**Revenue**

Huahong recorded revenues of RMB552.6 million, RMB479.1 million, RMB457.2 million, RMB132.8 million and RMB146.4 million for each of the years ended 31 December 2012, 2013, 2014, and for the four months ended 30 April 2014 and 2015, respectively, which were mainly derived from the sale of integrated circuit products.

The revenue decreased by 13.3% for the year ended 31 December 2013 as compared to the year ended 31 December 2012. This was mainly due to the fact that for the year ended 31 December 2012, Huahong recorded a significant increase in revenue from the sale of SIM cards from the disposal of large quantities of SIM cards on hand in anticipation of the technology transformation of SIM cards in 2013.

The revenue decreased by 4.6% for the year ended 31 December 2014 as compared to the year ended 31 December 2013 was mainly due to a decrease in revenue from the sale of identity cards. As the replacement of new identity cards passed its peak and returned to a relatively normal level, the sale of identity cards decreased significantly. However, the boost in the sale of bank cards had reduced some of the impact caused by the decrease in revenue from the sale of identity cards.

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## **APPENDIX I      MANAGEMENT DISCUSSION AND ANALYSIS OF HUAHONG**

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The revenue increased by 10.2% for the four months ended 30 April 2015 as compared to the four months ended 30 April 2014. This was mainly due to increased revenues from the sale of bank cards in 2015.

### **Cost of sales**

Huahong incurred cost of sales of RMB407.6 million, RMB333.3 million, RMB330.6 million, RMB96.4 million and RMB117.6 million for each of the years ended 31 December 2012, 2013, 2014, and for the four months ended 30 April 2014 and 2015, respectively. Cost of sales comprises mainly of raw materials and consumables used and employee benefit expenses.

During the period under review, the overall cost of production generally increased and the fluctuation in cost of sales was mainly driven by the costs of integrated circuit products sold.

### **Gross profit**

As a result of the above, Huahong recorded a gross profit of RMB145.0 million, RMB145.8 million, RMB126.5 million, RMB36.4 million and RMB28.8 million. The gross profit margin was 26.2%, 30.4%, 27.7%, 27.4% and 19.7% for each of the years ended 31 December 2012, 2013, 2014, and for the four months ended 30 April 2014 and 2015, respectively.

During the period under review, the market price competition within the industry intensified and have exerted pressure on the gross profit margin of Huahong.

### **Other income and gains – net**

Huahong recorded other income and gains – net of RMB28.2 million, RMB55.1 million, RMB82.7 million, RMB5.8 million and RMB15.2 million for each of the years ended 31 December 2012, 2013, 2014, and for the four months ended 30 April 2014 and 2015, respectively.

Other income and gains – net comprised mainly of government grants, which was RMB23.4 million, RMB47.2 million, RMB63.8 million, RMB1.2 million and RMB14.1 million for each of the years ended 31 December 2012, 2013, 2014, and for the four months ended 30 April 2014 and 2015, respectively. The fluctuation in other income and gains-net was mainly driven by the amount of government grants recognised as income. The government grants recognised as income fluctuated as a result of variations in government subsidies for research and development costs incurred. Government grants recognised as income increased significantly to RMB14.1 million for the four months ended 30 April 2015 as a result of more government subsidies for research and development costs incurred during the period in 2015.

**Selling and marketing costs**

Huahong incurred selling and marketing costs of RMB19.5 million, RMB17.3 million, RMB21.7 million, RMB6.6 million and RMB5.9 million for each of the years ended 31 December 2012, 2013, 2014, and for the four months ended 30 April 2014 and 2015, respectively.

Selling and marketing costs comprise mainly of employee benefit expenses and travelling expenses. As a percentage to revenue, selling and marketing costs represented 3.5%, 3.6%, 4.8%, 5.0% and 4.1% of the revenue recorded for each of the years ended 31 December 2012, 2013, 2014, and for the four months ended 30 April 2014 and 2015, respectively. The increase in selling and marketing costs for the year ended 31 December 2014 and for the four months ended 30 April 2015 as compared to the year ended 31 December 2013 was mainly due to an increase in marketing effort to promote the new social security cards and residence permits.

**Administrative expenses**

Huahong incurred administrative expenses of RMB116.8 million, RMB124.0 million, RMB138.4 million, RMB43.4 million and RMB40.3 million for each of the years ended 31 December 2012, 2013, 2014, and for the four months ended 30 April 2014 and 2015, respectively.

The increase in administrative expenses was mainly due to an increase in research and development costs, level of wages within the industry and overall operating costs. As a percentage to revenue, research and development costs represented 17.5%, 21.8%, 25.1%, 27.0% and 25.3% of the revenue recorded for each of the years ended 31 December 2012, 2013, 2014, and for the four months ended 30 April 2014 and 2015, respectively. Research and development costs were mainly incurred in the development of public transport cards, residence permits, SIM cards and bank cards.

The decrease in administrative expenses for the four months ended 30 April 2015 as compared to the four months ended 30 April 2014 was mainly due to the implementation of cost control measures in 2015 which led to a decrease in overall administrative expenses.

**Profit/(loss) for the years/periods**

As a result of the above, Huahong recorded a profit of RMB35.1 million, a profit of RMB64.2 million, a profit of RMB56.1 million, a loss of RMB2.8 million and a loss of RMB2.3 million for each of the years ended 31 December 2012, 2013, 2014, and for the four months ended 30 April 2014 and 2015, respectively.

**Liquidity and financial resources**

Total assets of Huahong were RMB838.4 million, RMB797.4 million, RMB652.0 million, and RMB629.6 million as at 31 December 2012, 2013, 2014 and 30 April 2015, respectively.

***Non-current assets***

Non-current assets of Huahong were RMB22.4 million, RMB43.2 million, RMB48.2 million, and RMB48.9 million as at 31 December 2012, 2013, 2014 and 30 April 2015, respectively. Non-current assets of Huahong comprise mainly of properties, plant and equipment.

***Current assets***

Current assets of Huahong were RMB816.0 million, RMB754.2 million, RMB603.8 million, and RMB580.7 million as at 31 December 2012, 2013, 2014 and 30 April 2015, respectively. Current assets of Huahong comprise mainly of (i) trade and other receivables; (ii) short-term deposits and (iii) cash and cash equivalents.

The decreasing trend in current assets was mainly due to (i) the payment of an aggregate of RMB237.7 million as dividends and (ii) the acquisition of properties of RMB29.8 million to meet its research and development and marketing requirements.

In order to maximise the return on cash on hand:

- (i) Huahong purchased wealth management products issued by financial institutions in the PRC. The maximum amount invested in 2013 and 2014 were RMB50.2 million and RMB156.7 million, respectively. The principal sums under these wealth management products were protected with expected returns ranging from 4.7% to 5.0% per annum.
- (ii) Huahong provided an entrusted loan of RMB50.0 million and RMB50.0 million to Shenzhen Aihua Electronics Co., Ltd and Dongguan CEC Aihua Electronics Co., Ltd, respectively in 2014. These entrusted loans were for a period of 6 months, secured and at an interest rate of 5.2% per annum.

***Liabilities***

Total liabilities of Huahong were RMB377.0 million, RMB319.3 million, RMB308.0 million, and RMB287.8 million as at 31 December 2012, 2013, 2014 and 30 April 2015, respectively.

The decreasing trend in total liabilities was mainly due to the decrease in deferred government grants, the amounts of which were mainly various subsidies received from local government authorities for financing various research and development projects conducted by Huahong, from RMB136.9 million to RMB108.2 million to RMB58.3 million and to RMB47.7 million as at 31 December 2012, 2013 and 2014 and 30 April 2015, respectively. As more research and development costs that deferred government grants intended to compensate was incurred during the period under review, more deferred government grants was transferred from liabilities to profit or loss.

***Ratios***

As at 31 December 2012, 2013, 2014 and 30 April 2015, Huahong had current ratios (being current assets over current liabilities) of 2.2 times, 2.4 times, 2.0 times and 2.0 times, respectively.

As at 31 December 2012, 2013, 2014 and 30 April 2015, Huahong had gearing ratio (being total liabilities over total equity) of 81.7%, 66.8%, 89.5% and 84.2%, respectively. There was a decrease in deferred government grants and trade and other payables which led to a decrease in total liabilities in 2013, while total equity remained more or less the same in 2013. This translated into a lower 66.8% gearing ratio in 2013. There was payment of dividends out of retained earnings which led to a decrease in total equity in 2014, while total liabilities remained more or less the same in 2014. This translated into a higher 89.5% gearing ratio in 2014.

**Employee and remuneration policies**

Huahong had 373, 416, 439 and 437 employees as at 31 December 2012, 2013, 2014 and 30 April 2015, respectively. They were remunerated on the basis of performance and experience and such remuneration is reviewed regularly with reference to industry practices. The employee benefits of Huahong include pension obligations, employee leave entitlements and bonus plans. Employee benefit expenses of Huahong for the years ended 31 December 2012, 2013, 2014, and for the four months ended 30 April 2014 and 2015, were RMB68.7 million, RMB73.6 million, RMB70.0 million, RMB24.8 million and RMB23.4 million, respectively.

**Foreign exchange exposure**

The operations of Huahong are principally conducted in the PRC and the financial information of Huahong is presented in Renminbi. As such, Huahong considered that it did not have any material exposure to fluctuations in exchange rate and hence no hedging measures were taken.

**Acquisition and disposal**

During the years ended 31 December 2012, 2013, 2014, and for the four months ended 30 April 2014 and 2015, there were no material acquisitions and disposals of any subsidiaries, joint ventures and associated companies by Huahong.

**Prospects and outlook**

Going forward, on the one hand, the Group will continue to adhere to its independent innovation development strategy, increase its investments in science and technology, and actively expand into new smart card application businesses such as financial security and other chip design segments. On the other hand, it will pursue development opportunities in the integrated circuits design sector and strive to maintain its leading position.

The electronic information technology industrial park market in the PRC is still at its initial development stage. With the launch of new supportive policies by the PRC government, such as the “Policies regarding the support for the development of the State’s information technology bases and industrial parks”, the comprehensive supporting facilities within the industrial parks and the funding obtained from the issue of the unsecured bonds in 2014 will serve as catalysts for the sustainable development of these industrial parks.

Further, Huahong is a leading supplier of contact, contactless and dual-interface integrated circuit chips in the PRC. Huahong is also well-positioned to tap into the PRC dual-interface financial security solutions and services market. In order to maximise the opportunities that are being presented to Huahong, there are plans to develop Huahong under a three-pronged strategy to consolidate and enhance its leading position in the industry and to delivering growth for its shareholders:

- 1) persist in independent technology innovation;
- 2) facilitate organic growth; and
- 3) intensify pace of research and product commercialization.

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## **APPENDIX I      MANAGEMENT DISCUSSION AND ANALYSIS OF HUAHONG**

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With Huahong's strong presence in the PRC integrated circuits industry, the Shanghai Huahong Acquisition, the Group will be well-positioned to swiftly capitalise on the enormous market opportunities created by the development of the integrated circuit industry.

With the opportunities that are presented and the strategies that are to be adopted as well as the support from CEC, the Group's electronic information technology industrial parks will eventually be transformed into fully-functional eco-wisdom electronics cities, which will ensure the Group's sustainable growth.

Given the favorable policies that are being launched to support the industry, the enormous market opportunities created by the development of the integrated circuits industry, the collaboration and integration of businesses between Huahong and Huada Electronics, the Board is confident that the Enlarged Group will create sustainable positive returns for Shareholders.

**AUDITED CONSOLIDATED FINANCIAL INFORMATION OF THE GROUP FOR EACH OF THE YEARS ENDED 31 DECEMBER 2012, 2013 AND 2014**

Financial information of the Group for each of the years ended 31 December 2012, 2013 and 2014 is disclosed on pages 37 to 98 of the annual report of the Company for the year ended 31 December 2012 published on 7 March 2013, pages 40 to 103 of the annual report of the Company for the year ended 31 December 2013 published on 17 April 2014 and pages 47 to 142 of the annual report of the Company for the year ended 31 December 2014 published on 29 April 2015, respectively, which are available on the website of the Stock Exchange ([www.hkexnews.hk](http://www.hkexnews.hk)) and the website of the Company ([www.cecholding.com](http://www.cecholding.com)).

The links to the annual reports of the Company for each of the years ended 31 December 2012, 2013 and 2014, respectively, are set out below:

2012 <http://www.hkexnews.hk/listedco/listconews/SEHK/2013/0307/LTN20130307335.pdf>

2013 <http://www.hkexnews.hk/listedco/listconews/SEHK/2014/0417/LTN20140417556.pdf>

2014 <http://www.hkexnews.hk/listedco/listconews/SEHK/2015/0429/LTN20150429733.pdf>

**Selected consolidated financial information of the Group for each of the years ended 31 December 2014 and 2013*****Consolidated balance sheets***

|                   | <b>As at 31 December</b> |                                             |
|-------------------|--------------------------|---------------------------------------------|
|                   | <b>2014</b>              | <b>2013</b>                                 |
|                   | <i>HK\$'000</i>          | <i>HK\$'000</i><br>(Restated <sup>1</sup> ) |
| Total assets      | 6,726,268                | 2,623,028                                   |
| Total liabilities | 5,624,438                | 1,411,212                                   |
| Total equity      | <u>1,101,830</u>         | <u>1,211,816</u>                            |

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**APPENDIX II****FINANCIAL INFORMATION OF THE GROUP**

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***Consolidated income statements***

|                                                              | <b>Year ended 31 December</b> |                                             |
|--------------------------------------------------------------|-------------------------------|---------------------------------------------|
|                                                              | <b>2014</b>                   | <b>2013</b>                                 |
|                                                              | <i>HK\$'000</i>               | <i>HK\$'000</i><br>(Restated <sup>1</sup> ) |
| Revenue                                                      | 1,357,062                     | 1,321,606                                   |
| Profit for the year attributable to<br>owners of the Company | <u>170,108</u>                | <u>291,966</u>                              |

***Consolidated statements of cash flows***

|                                                        | <b>Year ended 31 December</b> |                                             |
|--------------------------------------------------------|-------------------------------|---------------------------------------------|
|                                                        | <b>2014</b>                   | <b>2013</b>                                 |
|                                                        | <i>HK\$'000</i>               | <i>HK\$'000</i><br>(Restated <sup>1</sup> ) |
| Net cash (used in)/generated from operating activities | (193,354)                     | 305,612                                     |
| Net cash used in investing activities                  | (4,038,122)                   | (59,226)                                    |
| Net cash generated from/(use in) financing activities  | <u>3,974,790</u>              | <u>(33,665)</u>                             |
| Net (decrease)/increase in cash and cash equivalents   | <u>(256,686)</u>              | <u>212,721</u>                              |

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<sup>1</sup> The acquisition of CEC Technology was completed in June 2014. As both the Company and CEC Technology are under common control of CEC, these consolidated financial statements have been prepared using the principles of merger accounting, as prescribed in HKAG 5. These consolidated financial statements include the results and financial position of the companies comprising CEC Technology and its subsidiaries as if the acquisition of CEC Technology had occurred at previous balance sheet dates presented. Comparative figures for the year ended 31 December 2013 and at 31 December 2013 have been restated on such basis.

*The following is the text of a report received from the Company's reporting accountant, PricewaterhouseCoopers, Certified Public Accountants, Hong Kong, for the purpose of incorporation in this circular.*



羅兵咸永道

27 October 2015

*The Directors*

China Electronics Corporation Holdings Company Limited

Dear Sirs,

We report on the financial information of Shanghai Huahong Integrated Circuit Co., Ltd ("Huahong"), which comprises the balance sheets of Huahong as at 31 December 2012, 2013 and 2014 and 30 April 2015, and the statements of comprehensive income, the statements of changes in equity and the cash flow statements of Huahong for each of the years ended 31 December 2012, 2013 and 2014 and the four months ended 30 April 2015 (the "Relevant Periods") and a summary of significant accounting policies and other explanatory information. This financial information has been prepared by the directors of China Electronics Corporation Holdings Company Limited (the "Company") and is set out in Sections I to II below for inclusion in Appendix III to the circular of the Company dated 27 October 2015 (the "Circular") in connection with the proposed acquisition of Huahong by the Company.

Huahong was incorporated in the People's Republic of China (the "PRC") on 14 December 1998 as a company with limited liability under the Companies Law of the PRC.

As at the date of this report, Huahong has interest in the joint venture as set out in Note 12 of Section II below.

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The directors of Huahong during the Relevant Periods are responsible for the preparation of the financial statements of Huahong that give a true and fair view in accordance with Hong Kong Financial Reporting Standards (“HKFRSs”) issued by the Hong Kong Institute of Certified Public Accountants (the “HKICPA”) (the “Underlying Financial Statements”), and for such internal control as the directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error. PricewaterhouseCoopers Zhong Tian LLP has audited the underlying Financial Statements in accordance with Hong Kong Standards on Auditing (the “HKSA”) issued by the HKICPA pursuant to separated terms of engagement.

The financial information has been prepared based on the underlying financial statements of Huahong with no adjustment made thereon.

### **DIRECTORS' RESPONSIBILITY FOR THE FINANCIAL INFORMATION**

The directors of the Company are responsible for the preparation of the financial information that gives a true and fair view in accordance with HKFRSs and accounting policies adopted by the Company and its subsidiaries (together, the “Group”) as set out in the annual report of the Company for the year ended 31 December 2014.

### **REPORTING ACCOUNTANT'S RESPONSIBILITY**

Our responsibility is to express an opinion on the financial information and to report our opinion to you. We carried out our procedures in accordance with the Auditing Guideline 3.340 “Prospectuses and the Reporting Accountant” issued by the HKICPA.

### **OPINION**

In our opinion, the financial information gives, for the purpose of this report, a true and fair view of the state of affairs of Huahong as at 31 December 2012, 2013 and 2014 and 30 April 2015 and of Huahong's results and cash flows for the Relevant Periods then ended.

### **REVIEW OF STUB PERIOD COMPARATIVE FINANCIAL INFORMATION**

We have reviewed the stub period comparative financial information set out in Sections I to II below included in Appendix III to the Circular which comprises the statement of comprehensive income, the statement of changes in equity and the cash flow statement of Huahong for the four months ended 30 April 2014 and a summary of significant accounting policies and other explanatory information (the “Stub Period Comparative Financial Information”).

The directors of the Company are responsible for the preparation and presentation of the Stub Period Comparative Financial Information in accordance with the accounting policies set out in Note 2 of Section II below and the accounting policies adopted by the Group as set out in the annual report of the Company for the year ended 31 December 2014.

Our responsibility is to express a conclusion on the Stub Period Comparative Financial Information based on our review. We conducted our review in accordance with Hong Kong Standard on Review Engagements 2410, “Review of Interim Financial Information Performed by the Independent Auditor of the Entity” issued by the HKICPA. A review of Stub Period Comparative Financial Information consists of making inquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with Hong Kong Standards on Auditing and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

Based on our review, nothing has come to our attention that causes us to believe that the Stub Period Comparative Financial Information, for the purpose of this report, is not prepared, in all material respects, in accordance with the accounting policies set out in Note 2 of Section II below.

## I. FINANCIAL INFORMATION

The following is the financial information of Huahong (the “Financial Information”) prepared by the directors of the Company as at 31 December 2012, 2013 and 2014 and 30 April 2015 and for each of the years ended 31 December 2012, 2013 and 2014 and for the four months ended 30 April 2014 and 2015 (the “Relevant Periods”).

## Statements of Comprehensive Income

|                                                                                    |      | Year ended 31 December |               |                | Four months ended<br>30 April |                |
|------------------------------------------------------------------------------------|------|------------------------|---------------|----------------|-------------------------------|----------------|
|                                                                                    |      | 2012                   | 2013          | 2014           | 2014                          | 2015           |
|                                                                                    | Note | RMB'000                | RMB'000       | RMB'000        | RMB'000<br>(Unaudited)        | RMB'000        |
| <b>Revenue</b>                                                                     | 5    | 552,605                | 479,127       | 457,169        | 132,766                       | 146,368        |
| Cost of sales                                                                      | 7    | (407,649)              | (333,284)     | (330,642)      | (96,400)                      | (117,573)      |
| <b>Gross profit</b>                                                                |      | 144,956                | 145,843       | 126,527        | 36,366                        | 28,795         |
| Other income and gains – net                                                       | 6    | 28,201                 | 55,090        | 82,712         | 5,823                         | 15,214         |
| Selling and marketing costs                                                        | 7    | (19,541)               | (17,263)      | (21,730)       | (6,573)                       | (5,945)        |
| Administrative expenses                                                            | 7    | (116,833)              | (124,003)     | (138,367)      | (43,411)                      | (40,298)       |
| <b>Operating profit/(loss)</b>                                                     |      | 36,783                 | 59,667        | 49,142         | (7,795)                       | (2,234)        |
| Finance income                                                                     | 9    | 3,647                  | 4,571         | 2,105          | 774                           | 446            |
| Share of result of<br>a joint venture                                              |      | –                      | –             | 553            | –                             | (473)          |
| <b>Profit/(loss) before<br/>taxation</b>                                           |      | 40,430                 | 64,238        | 51,800         | (7,021)                       | (2,261)        |
| Taxation                                                                           | 10   | (5,345)                | –             | 4,269          | 4,269                         | –              |
| <b>Profit/(loss) for the year/<br/>period</b>                                      |      | <u>35,085</u>          | <u>64,238</u> | <u>56,069</u>  | <u>(2,752)</u>                | <u>(2,261)</u> |
| <b>Other comprehensive<br/>income</b>                                              |      | –                      | –             | –              | –                             | –              |
| <b>Total comprehensive<br/>income/(loss) attributable<br/>to owners of Huahong</b> |      | <u>35,085</u>          | <u>64,238</u> | <u>56,069</u>  | <u>(2,752)</u>                | <u>(2,261)</u> |
| <b>Dividends</b>                                                                   | 21   | <u>69,051</u>          | <u>47,541</u> | <u>190,165</u> | <u>31,694</u>                 | –              |

**Balance Sheets**

|                                     |      | As at 31 December     |                       |                       | As at                 |
|-------------------------------------|------|-----------------------|-----------------------|-----------------------|-----------------------|
|                                     |      | 2012                  | 2013                  | 2014                  | 30 April              |
|                                     | Note | RMB'000               | RMB'000               | RMB'000               | 2015                  |
|                                     |      |                       |                       |                       | RMB'000               |
| <b>ASSETS</b>                       |      |                       |                       |                       |                       |
| <b>Non-current assets</b>           |      |                       |                       |                       |                       |
| Property, plant and equipment       | 11   | 12,408                | 43,236                | 42,521                | 43,746                |
| Investment in a joint venture       | 12   | –                     | –                     | 5,653                 | 5,180                 |
| Long-term deposits                  | 17   | 10,000                | –                     | –                     | –                     |
|                                     |      | <u>22,408</u>         | <u>43,236</u>         | <u>48,174</u>         | <u>48,926</u>         |
| <b>Current assets</b>               |      |                       |                       |                       |                       |
| Inventories                         | 13   | 87,266                | 71,845                | 97,906                | 157,033               |
| Trade and other receivables         | 14   | 269,086               | 235,906               | 236,368               | 288,292               |
| Available-for-sale financial assets | 15   | –                     | 50,225                | 51,334                | –                     |
| Restricted deposits                 | 16   | 4,579                 | 225                   | 2,201                 | –                     |
| Short-term deposits                 | 17   | 76,064                | 103,254               | 1,000                 | 1,000                 |
| Cash and cash equivalents           | 18   | 378,987               | 292,737               | 215,021               | 134,338               |
|                                     |      | <u>815,982</u>        | <u>754,192</u>        | <u>603,830</u>        | <u>580,663</u>        |
| <b>Total assets</b>                 |      | <u><u>838,390</u></u> | <u><u>797,428</u></u> | <u><u>652,004</u></u> | <u><u>629,589</u></u> |

# APPENDIX III

# ACCOUNTANT'S REPORT OF HUAHONG

|                                                  |      | As at 31 December     |                       |                       | As at                 |
|--------------------------------------------------|------|-----------------------|-----------------------|-----------------------|-----------------------|
|                                                  |      | 2012                  | 2013                  | 2014                  | 30 April              |
|                                                  | Note | RMB'000               | RMB'000               | RMB'000               | 2015                  |
|                                                  |      |                       |                       |                       | RMB'000               |
| <b>EQUITY AND LIABILITIES</b>                    |      |                       |                       |                       |                       |
| <b>Equity</b>                                    |      |                       |                       |                       |                       |
| Paid-in capital                                  | 19   | 158,471               | 158,471               | 158,471               | 158,471               |
| Other reserves                                   | 20   | 182,189               | 189,764               | 189,764               | 189,764               |
| Retained earnings/<br>(Accumulated losses)       |      | 120,745               | 129,867               | (4,229)               | (6,490)               |
| <b>Total equity</b>                              |      | <u>461,405</u>        | <u>478,102</u>        | <u>344,006</u>        | <u>341,745</u>        |
| <b>Liabilities</b>                               |      |                       |                       |                       |                       |
| <b>Current liabilities</b>                       |      |                       |                       |                       |                       |
| Amount due to ultimate<br>holding company        | 22   | –                     | 15,000                | 15,000                | 15,000                |
| Deferred government grants                       | 23   | 136,894               | 108,245               | 58,307                | 47,724                |
| Advances from customers                          |      | 153                   | 356                   | 2,744                 | 1,563                 |
| Trade and other payables                         | 24   | 218,135               | 180,144               | 218,767               | 210,999               |
| Income tax payable                               |      | 21,803                | 15,581                | 13,180                | 12,558                |
| <b>Total liabilities</b>                         |      | <u>376,985</u>        | <u>319,326</u>        | <u>307,998</u>        | <u>287,844</u>        |
| <b>Total equity and liabilities</b>              |      | <u><u>838,390</u></u> | <u><u>797,428</u></u> | <u><u>652,004</u></u> | <u><u>629,589</u></u> |
| <b>Net current assets</b>                        |      | <u><u>438,997</u></u> | <u><u>434,866</u></u> | <u><u>295,832</u></u> | <u><u>292,819</u></u> |
| <b>Total assets less current<br/>liabilities</b> |      | <u><u>461,405</u></u> | <u><u>478,102</u></u> | <u><u>344,006</u></u> | <u><u>341,745</u></u> |

## Statements of Changes in Equity

|                               |      | Paid-in<br>capital | Other<br>reserves | Retained<br>earnings/<br>(Accumulated<br>losses) | Total          |
|-------------------------------|------|--------------------|-------------------|--------------------------------------------------|----------------|
|                               | Note | RMB'000            | RMB'000           | RMB'000                                          | RMB'000        |
| <b>At 1 January 2012</b>      |      | 131,949            | 114,010           | 162,971                                          | 408,930        |
| Total comprehensive income    |      | –                  | –                 | 35,085                                           | 35,085         |
| Capital injection             |      | 26,522             | 59,919            | –                                                | 86,441         |
| Transfer to statutory reserve |      | –                  | 8,260             | (8,260)                                          | –              |
| Dividends                     | 21   | –                  | –                 | (69,051)                                         | (69,051)       |
| <b>At 31 December 2012</b>    |      | <u>158,471</u>     | <u>182,189</u>    | <u>120,745</u>                                   | <u>461,405</u> |
| <b>At 1 January 2013</b>      |      | 158,471            | 182,189           | 120,745                                          | 461,405        |
| Total comprehensive income    |      | –                  | –                 | 64,238                                           | 64,238         |
| Transfer to statutory reserve |      | –                  | 7,575             | (7,575)                                          | –              |
| Dividends                     | 21   | –                  | –                 | (47,541)                                         | (47,541)       |
| <b>At 31 December 2013</b>    |      | <u>158,471</u>     | <u>189,764</u>    | <u>129,867</u>                                   | <u>478,102</u> |
| <b>At 1 January 2014</b>      |      | 158,471            | 189,764           | 129,867                                          | 478,102        |
| Total comprehensive income    |      | –                  | –                 | 56,069                                           | 56,069         |
| Dividends                     | 21   | –                  | –                 | (190,165)                                        | (190,165)      |
| <b>At 31 December 2014</b>    |      | <u>158,471</u>     | <u>189,764</u>    | <u>(4,229)</u>                                   | <u>344,006</u> |
| <b>At 1 January 2015</b>      |      | 158,471            | 189,764           | (4,229)                                          | 344,006        |
| Total comprehensive loss      |      | –                  | –                 | (2,261)                                          | (2,261)        |
| <b>At 30 April 2015</b>       |      | <u>158,471</u>     | <u>189,764</u>    | <u>(6,490)</u>                                   | <u>341,745</u> |
| <b>(Unaudited)</b>            |      |                    |                   |                                                  |                |
| <b>At 1 January 2014</b>      |      | 158,471            | 189,764           | 129,867                                          | 478,102        |
| Total comprehensive loss      |      | –                  | –                 | (2,752)                                          | (2,752)        |
| Dividends                     | 21   | –                  | –                 | (31,694)                                         | (31,694)       |
| <b>At 30 April 2014</b>       |      | <u>158,471</u>     | <u>189,764</u>    | <u>95,421</u>                                    | <u>443,656</u> |

## Cash Flow Statements

|                                             | <i>Note</i> | Year ended 31 December |                   |                   | Four months ended<br>30 April |                   |
|---------------------------------------------|-------------|------------------------|-------------------|-------------------|-------------------------------|-------------------|
|                                             |             | 2012                   | 2013              | 2014              | 2014                          | 2015              |
|                                             |             | <i>RMB'000</i>         | <i>RMB'000</i>    | <i>RMB'000</i>    | <i>RMB'000</i>                | <i>RMB'000</i>    |
|                                             |             |                        |                   |                   | (Unaudited)                   |                   |
| <b>Cash flows from operating activities</b> |             |                        |                   |                   |                               |                   |
| Cash generated from/                        |             |                        |                   |                   |                               |                   |
| (used in) operations                        | 25          | 99,501                 | 47,435            | 11,350            | (45,194)                      | (131,081)         |
| Income tax paid                             |             | (5,655)                | (6,222)           | (2,401)           | (982)                         | (622)             |
| Income tax refunded                         |             | —                      | —                 | 4,269             | 4,269                         | —                 |
|                                             |             | <u>          </u>      | <u>          </u> | <u>          </u> | <u>          </u>             | <u>          </u> |
| <b>Net cash generated from/</b>             |             |                        |                   |                   |                               |                   |
| <b>  (used in) operating</b>                |             |                        |                   |                   |                               |                   |
| <b>  activities</b>                         |             | <u>93,846</u>          | <u>41,213</u>     | <u>13,218</u>     | <u>(41,907)</u>               | <u>(131,703)</u>  |
| <b>Cash flows from investing activities</b> |             |                        |                   |                   |                               |                   |
| Interest income received on                 |             |                        |                   |                   |                               |                   |
| short-term and long-term                    |             |                        |                   |                   |                               |                   |
| deposits                                    |             | 1,541                  | 4,166             | 5,221             | 1,538                         | 109               |
| Interest income received                    |             |                        |                   |                   |                               |                   |
| on available-for-sale                       |             |                        |                   |                   |                               |                   |
| financial assets                            |             | —                      | —                 | 1,985             | 1,383                         | 2,137             |
| Interest income received on                 |             |                        |                   |                   |                               |                   |
| entrusted loan                              |             | —                      | —                 | 2,658             | —                             | —                 |
| Interest income received on                 |             |                        |                   |                   |                               |                   |
| deferred consideration                      |             |                        |                   |                   |                               |                   |
| receivable                                  |             | 2,545                  | —                 | —                 | —                             | —                 |
| Proceeds from disposal                      |             |                        |                   |                   |                               |                   |
| of a subsidiary                             |             | 32,273                 | —                 | —                 | —                             | —                 |
| Purchase of property, plant                 |             |                        |                   |                   |                               |                   |
| and equipment                               |             | (4,995)                | (36,340)          | (6,185)           | (1,764)                       | (3,427)           |
| Proceeds from disposal                      |             |                        |                   |                   |                               |                   |
| of property, plant and                      |             |                        |                   |                   |                               |                   |
| equipment                                   |             | 68                     | 88                | 374               | 3                             | —                 |
| Investment in a joint                       |             |                        |                   |                   |                               |                   |
| venture using equity                        |             |                        |                   |                   |                               |                   |
| accounting                                  |             | —                      | —                 | (5,100)           | —                             | —                 |
| Purchase for available-for-                 |             |                        |                   |                   |                               |                   |
| sale financial assets                       |             | —                      | (50,000)          | (206,730)         | (156,730)                     | —                 |
| Proceeds from disposal                      |             |                        |                   |                   |                               |                   |
| of available-for-sale                       |             |                        |                   |                   |                               |                   |
| financial assets                            |             | —                      | —                 | 206,730           | 150,000                       | 50,000            |

# APPENDIX III

# ACCOUNTANT'S REPORT OF HUAHONG

|                                                                | Year ended 31 December   |                 |                  | Four months ended<br>30 April |                |
|----------------------------------------------------------------|--------------------------|-----------------|------------------|-------------------------------|----------------|
|                                                                | 2012                     | 2013            | 2014             | 2014                          | 2015           |
| Note                                                           | RMB'000                  | RMB'000         | RMB'000          | RMB'000                       | RMB'000        |
|                                                                |                          |                 |                  | (Unaudited)                   |                |
| Entrusted loan to related parties                              | –                        | –               | (100,000)        | –                             | –              |
| Reclaim of entrusted loan                                      | –                        | –               | 100,000          | –                             | –              |
| (Increase)/decrease in short-term and long-term deposits       | (16,064)                 | (17,190)        | 102,254          | (2,000)                       | –              |
| Decrease/(increase) in restricted deposits                     | 10,412                   | 4,354           | (1,976)          | –                             | 2,201          |
| <b>Net cash generated from/ (used in) investing activities</b> | <u>25,780</u>            | <u>(94,922)</u> | <u>99,231</u>    | <u>(7,570)</u>                | <u>51,020</u>  |
| <b>Cash flows from financing activities</b>                    |                          |                 |                  |                               |                |
| Dividends paid                                                 | (69,051)                 | (47,541)        | (190,165)        | (31,694)                      | –              |
| Capital contribution from owners of Huahong                    | 86,441                   | –               | –                | –                             | –              |
| Cash received from ultimate holding company                    | –                        | 15,000          | –                | –                             | –              |
| <b>Net cash generated from/ (used in) financing activities</b> | <u>17,390</u>            | <u>(32,541)</u> | <u>(190,165)</u> | <u>(31,694)</u>               | <u>–</u>       |
| <b>Net increase/(decrease) in cash and cash equivalents</b>    | 137,016                  | (86,250)        | (77,716)         | (81,171)                      | (80,683)       |
| Cash and cash equivalents at beginning of the year/ period     | <u>241,971</u>           | <u>378,987</u>  | <u>292,737</u>   | <u>292,737</u>                | <u>215,021</u> |
| <b>Cash and cash equivalents at end of the year/ period</b>    | <u>18</u> <u>378,987</u> | <u>292,737</u>  | <u>215,021</u>   | <u>211,566</u>                | <u>134,338</u> |

**II. NOTES TO FINANCIAL INFORMATION****1. General information**

Huahong is principally engaged in design and sale of integrated circuit chips in People's Republic of China (the "PRC"). The ultimate controlling company of Huahong is CEC.

The Financial Information is presented in the units of Renminbi ("RMB"), unless otherwise stated.

**2. Summary of significant accounting policies**

The principal accounting policies applied in the preparation of the Financial Information are set out below. These policies have been consistently applied to the Relevant Periods.

***2.1 Basis of preparation***

The Financial Information has been prepared in accordance with Hong Kong Financial Reporting Standards ("HKFRS") issued by the Hong Kong Institute of Certified Public Accountants and under the historical cost convention as modified by the revaluation of available-for-sale financial assets which are carried at fair value. Huahong adopts the going concern basis in preparing the Financial Information.

The preparation of Financial Information in conformity with HKFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgment in the process of applying Huahong's accounting policies. The areas involving a higher degree of judgment or complexity, or areas where assumptions and estimates are significant to the Financial Information are disclosed in Note 4.

*New and amendment to standards and interpretations*

All new standards, amendments to standards and interpretations which are mandatory for the Relevant Periods are applied to Huahong.

The following new standards and amendments to standards that are relevant to the operation of Huahong have been issued but are not effective and have not been early adopted:

|                                         |                                                                                                                             |
|-----------------------------------------|-----------------------------------------------------------------------------------------------------------------------------|
| HKAS 16 and<br>HKAS 38<br>(amendments)  | Clarification of acceptable methods of<br>depreciation and amortisation (effective from<br>1 January 2016)                  |
| HKFRS 9                                 | Financial instruments (effective from 1 January<br>2018)                                                                    |
| HKFRS 15                                | Revenue from contracts with customers (effective<br>from 1 January 2018)                                                    |
| HKAS 1<br>(amendments)                  | Disclosure initiative (effective from 1 January<br>2016)                                                                    |
| HKFRS 10 and<br>HKAS 28<br>(amendments) | Sale or contribution of assets between an investor<br>and its associate or joint venture (effective from<br>1 January 2016) |
| HKAS 27<br>(amendments)                 | Equity method in separate financial statements<br>(effective from 1 January 2016)                                           |
| Annual<br>improvements 2014             | Changes from the 2012-2014 cycle of the annual<br>improvements project (effective from 1 January<br>2016)                   |

Huahong is in the process of making an assessment of the impact of the above standards and amendments to standards to the Financial Information of Huahong in their initial applications.

## **2.2    *Joint arrangements***

Investments in joint arrangements are classified as either joint operations or joint ventures depending on the contractual rights and obligations of each investor. Huahong has assessed the nature of its joint arrangement and determined it to be a joint venture. Joint venture is accounted for using the equity method of accounting. Under the equity method, interest in a joint venture is initially recognised at cost and adjusted thereafter to recognise Huahong's share of post-acquisition profit or loss and movements in other comprehensive income. Huahong's investment in a joint venture includes goodwill identified on acquisition. Upon the acquisition of the ownership interest in a joint venture, any difference between the cost of the joint venture and Huahong's share of the net fair value of the joint venture's identifiable assets and liabilities is accounted for as goodwill. When Huahong's share of losses in a joint venture equals or exceeds its interests in the joint venture (which includes any long-term interests that, in substance, form part of Huahong's net investment in the joint venture), Huahong does not recognise further losses, unless it has incurred legal or constructive obligations or made payments on behalf of the joint venture.

Huahong determines at each reporting date whether there is any objective evidence that the investment in the joint venture is impaired. If this is the case, Huahong calculates the amount of impairment as the difference between the recoverable amount of the joint venture and its carrying value and recognises the amount adjacent to "share of result of a joint venture" in the statements of comprehensive income.

Unrealised gains on transactions between Huahong and its joint venture are eliminated to the extent of Huahong's interest in the joint venture. Unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. Accounting policies of the joint venture have been changed where necessary to ensure consistency with the policies adopted by Huahong.

## **2.3    *Segment reporting***

Operating segments are reported in a manner consistent with the internal reporting provided to the chief operating decision-maker. The chief operating decision-maker, who is responsible for allocating resources and assessing performance of the operating segments, has been identified as the board of directors that makes strategic decisions.

**2.4 Foreign currency translation***(a) Functional and presentation currency*

Items included in the Financial Information of Huahong are measured using the currency of the primary economic environment in which Huahong operates (the “functional currency”). The Financial Information is presented in RMB, which is Huahong’s functional currency and presentation currency.

*(b) Transactions and balances*

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the statements of comprehensive income.

Foreign exchange gains and losses that relate to cash and cash equivalents are presented in the statements of comprehensive income within “finance income”. All other foreign exchange gains and losses are presented in the statements of comprehensive income within “other income and gains – net”.

**2.5 Property, plant and equipment**

Property, plant and equipment are stated at historical cost less depreciation and any impairment losses. Historical cost includes expenditure that is directly attributable to the acquisition of the items.

Subsequent costs are included in the asset’s carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to Huahong and the cost of the item can be measured reliably. All other repairs and maintenance are expensed in the statements of comprehensive income during the Relevant Periods in which they are incurred.

Depreciation on property, plant and equipment is calculated using the straight-line method to allocate their cost less their residual values over their estimated useful lives, as follows:

|                         |                                                         |
|-------------------------|---------------------------------------------------------|
| Buildings               | 20 years                                                |
| Leasehold improvements  | 5 years or over the lease term,<br>whichever is shorter |
| Plant and machinery     | 3 – 5 years                                             |
| Motor vehicles          | 5 years                                                 |
| Furnitures and fixtures | 3 – 5 years                                             |

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at the end of each reporting period. An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount (*Note 2.6*).

Gains and losses on disposals or retirement are determined by comparing the proceeds with the carrying amount of the asset and are recognised within "other income and gains – net" in the statements of comprehensive income.

#### **2.6    *Impairment of non-financial assets***

Assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units). Non-financial assets other than goodwill that suffered an impairment are reviewed for possible reversal of the impairment at each reporting date.

## 2.7 *Financial assets*

### 2.7.1 *Classification*

Huahong classifies its financial assets into two categories: loans and receivables and available-for-sale financial assets. The classification depends on the purpose for which the financial assets were acquired. Management determines the classification of its financial assets at initial recognition.

#### (a) Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They are included in current assets, except for maturities greater than 1 year after the balance sheet date, which are classified as non-current assets. Huahong's loans and receivables comprise "trade and other receivables" (*Note 2.9*), "cash and cash equivalents" (*Note 2.10*), "short-term and long-term deposits" and "restricted deposits" in the balance sheet.

#### (b) Available-for-sale financial assets

Available-for-sale financial assets are non-derivatives financial assets that are either designated in this category or not classified in the other category. They are included in current assets when management intends to dispose of the investment within 1 year of the balance sheet date.

### 2.7.2 *Recognition and measurement*

Regular way purchases and sale of financial assets are recognised on the trade-date – the date on which Huahong commits to purchase or sell the asset. Investments are initially recognised at fair value plus transaction costs for all financial assets. Financial assets are derecognised when the rights to receive cash flows from the investments have expired or have been transferred and Huahong has transferred substantially all risks and rewards of ownership. Available-for-sale financial assets are subsequently carried at fair value. Loans and receivables are carried at amortised cost using the effective interest method.

Interest on available-for-sale debt instruments calculated using the effective interest method is recognised in the statements of comprehensive income as part of “other income and gains – net”.

#### *2.7.3 Impairment of financial assets*

Huahong assesses at each balance sheet date whether there is objective evidence that a financial asset or a group of financial assets is impaired. All impairment loss is recognised in the statements of comprehensive income. If, in a subsequent period, the fair value of a debt instrument classified as available-for-sale increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in profit or loss, the impairment loss is reversed through the statements of comprehensive income. Impairment testing of trade and other receivables is described in Note 2.9.

### **2.8 Inventories**

Inventories are stated at the lower of cost and net realisable value. Cost is determined using the weighted-average method. The cost of finished goods and work in progress comprises design costs, raw materials, direct labour, manufacturing cost of subcontractors, other direct costs and related production overheads (based on normal operating capacity). It excludes borrowing costs. Net realisable value is the estimated selling price in the ordinary course of business, less applicable variable selling expenses.

### **2.9 Trade and other receivables**

Trade receivables are amounts due from customers for merchandise sold in the ordinary course of business. If collection of trade and other receivables is expected in 1 year or less, they are classified as current assets. If not, they are presented as non-current assets. Trade and other receivables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method, less provision for impairment. A provision for impairment of trade and other receivables is established when there is objective evidence that Huahong will not be able to collect all amounts due according to the original terms of the receivables. Significant financial difficulty of the debtor, probability that the debtor will enter bankruptcy or financial reorganisation, and default or delinquency in payments are considered indicators that the receivable is impaired. The amount of the provision is the difference between the receivable's carrying amount and the present value of estimated future cash flows, discounted at the original effective interest rate. The carrying amount of the receivable is reduced through the use of an allowance account,

and the amount of the provision is recognised in the statements of comprehensive income within “administrative expenses”. When the receivable is uncollectible, it is written off against the allowance account for receivables. If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised (such as an improvement in the debtor’s credit rating), the reversal of the previously recognised impairment loss is recognised in the statements of comprehensive income.

### ***2.10 Cash and cash equivalents***

Cash and cash equivalents includes cash on hand, deposits held at call with banks and other financial institutions and other short-term highly liquid investments with original maturities of 3 months or less.

### ***2.11 Paid-in capital***

Paid-in capital is classified as equity. Incremental costs directly attributable to the issue of new shares are shown in equity as a deduction, net of tax, from the proceeds.

### ***2.12 Government grants***

Government grants are recognised at their fair values where there is a reasonable assurance that the government grant will be received and Huahong will comply with all attached conditions. Government grant relating to an expense item is deferred and recognised as other income in the statements of comprehensive income over the period necessary to match with the cost that it is intended to compensate.

### ***2.13 Trade payables***

Trade payables are obligations to pay for goods or services that have been acquired in the ordinary course of business from suppliers. Trade payables are classified as current liabilities if payment is due within 1 year or less. If not, they are presented as non-current liabilities. Trade payables are initially recognised at fair value and subsequently measured at amortised cost using the effective interest method.

**2.14 Current and deferred taxation**

The taxation expense comprises current and deferred taxation. Tax is recognised in the statements of comprehensive income, except to the extent that it relates to items recognised in other comprehensive income or directly in equity. In this case, the tax is also recognised in other comprehensive income or equity.

**(a) Current income tax**

The current income tax charge is calculated on the basis of the tax laws enacted or substantively enacted at the balance sheet date in the countries where Huahong operates and generates taxable income. Management periodically evaluates positions taken in tax returns with respect to situations in which applicable tax regulation is subject to interpretation. It establishes provisions where appropriate on the basis of amounts expected to be paid to the tax authorities.

**(b) Deferred taxation differences****(i) Inside basis differences**

Deferred tax is recognised, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the Financial Information. However, the deferred taxation is not recognised for if it arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit or loss. Deferred taxation is determined using the tax rates (and laws) that have been enacted or substantively enacted at the balance sheet date and are expected to apply when the related deferred tax asset is realised or the deferred tax liability is settled.

Deferred tax assets are recognised to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilized.

(ii) Outside basis differences

Deferred tax liabilities are provided on taxable temporary differences arising from investment in joint arrangement, except for deferred tax liability where the timing of the reversal of the temporary difference is controlled by Huahong and it is probable that the temporary difference will not reverse in the foreseeable future. Generally Huahong is unable to control the reversal of the temporary difference for joint arrangement. Only when there is an agreement in place that gives Huahong the ability to control the reversal of the temporary difference in the foreseeable future, deferred tax liability in relation to taxable temporary differences arising from the joint arrangement's undistributed profits is not recognised.

Deferred tax assets are recognised on deductible temporary differences arising from investments in joint arrangement only to the extent that it is probable the temporary difference will reverse in the future and there is sufficient taxable profit available against which the temporary difference can be utilised.

(c) *Offsetting*

Deferred tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets against current tax liabilities and when the deferred taxes assets and liabilities relate to income taxes levied by the same taxation authority on either the taxable entity or different taxable entities where there is an intention to settle the balances on a net basis.

**2.15 Provisions**

Provisions are recognised when Huahong has a present legal or constructive obligation as a result of past events; it is probable that an outflow of resources will be required to settle the obligation; and the amount has been reliably estimated. Provisions are not recognised for future operating losses.

Where there are a number of similar obligations, the likelihood that an outflow of resources will be required in settlement is determined by considering the class of obligations as a whole. A provision is recognised even if the likelihood of an outflow of resources with respect to any one item included in the same class of obligations may be small.

Provisions are measured at the present value of expenditures expected to be required to settle the obligation using a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the obligation. The increase in the provision due to passage of time is recognised as interest expense.

### **2.16 Employee benefits**

#### *(a) Pension obligations*

The employees of Huahong participate in the defined contribution retirement plans managed by the local government authorities. Huahong has to make contribution to staff retirement scheme managed by local government authorities in accordance with the relevant rules and regulations. Contributions to these schemes are charged to the statements of comprehensive income as and when incurred. Huahong has no legal or constructive obligations to pay further contributions.

#### *(b) Employee leave entitlements*

Employee entitlements to annual leave are recognised when they accrue to employees. A provision is made for the estimated liability for annual leave as a result of services rendered by employees up to the balance sheet date.

Employee entitlements to sick leave and maternity leave are not recognised until the time of leave.

#### *(c) Bonus plans*

The expected cost of bonuses is recognised as a liability when Huahong has a present legal or constructive obligation for payment of bonus as a result of services rendered by employees and a reliable estimate of the obligation can be made.

Liabilities for bonus plans are expected to be settled within 1 year and are measured at the amounts expected to be paid when they are settled.

***2.17 Contingent liabilities***

A contingent liability is a possible obligation that arises from past events and whose existence will only be confirmed by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of Huahong. It can also be a present obligation arising from past events that is not recognised because it is not probable that outflow of resources will be required or the amount of obligation cannot be measured reliably.

A contingent liability is not provided for as a provision but is disclosed in the notes to the Financial Information. When a change in the probability of an outflow of resources occurs so that the outflow is probable, they will then be recognised as a provision.

***2.18 Revenue recognition***

Revenue comprises the fair value of the consideration received or receivable for the sale of goods, net of value-added tax, returns, rebates and discounts. Revenue is recognised when the goods are delivered to customers, the customers have accepted the goods or the product quality inspection time period has lapsed and collectability of the related receivables is reasonably assured.

***2.19 Operating leases***

Leases in which substantially all the risks and rewards of ownership are retained by the lessor are classified as operating leases. Payments made under operating leases (net of any incentives received from the lessor) are charged to the statements of comprehensive income on a straight-line basis over the period of the lease.

***2.20 Research and development costs***

Research costs are expensed as incurred. Development costs that are directly attributable to the design and testing of identifiable and unique software products are recognised as intangible assets when the following criteria are met:

- it is technically feasible to complete the software product so that it will be available for use;
- management intends to complete the software product and use or sell it;

- there is an ability to use or sell the software product;
- it can be demonstrated how the software product will generate probable future economic benefits;
- adequate technical, financial and other resources to complete the development of the software product are available; and
- the expenditure attributable to the software product during its development can be reliably measured.

Other development costs that do not meet these criteria are recognised as an expense as incurred. Development costs previously recognised as an expense are not recognised as an asset in a subsequent period.

#### ***2.21 Interest income***

Interest income is recognised on a time-proportion basis, taking into account the principal amounts outstanding and the interest rates applicable.

#### ***2.22 Dividend distribution***

Dividend distribution to Huahong's shareholders is recognised as a liability in the Financial Information in the period in which the dividends are approved by Huahong's shareholders or directors, where appropriate.

### **3. Financial risk management**

#### ***3.1 Financial risk factors***

Huahong's activities expose it to a variety of financial risks: foreign exchange risk, market risk (mainly including cash flow and fair value interest rate risk), credit risk and liquidity risk. The management manages and monitors these exposures to ensure appropriate measures are implemented on a timely and effective manner.

*(a) Foreign exchange risk*

The foreign exchange risks of Huahong occurred due to the fact that Huahong had some business activities denominated in foreign currencies. Huahong's business activities are primarily exposed to foreign exchange risk in respect of United States dollar against RMB. Foreign exchange risk arises from future commercial transactions and recognised assets and liabilities that are denominated in a currency that is not the entity's functional currency. In additions, the conversion of RMB into foreign currencies is subject to the rules and regulations of foreign exchange control promulgated by the PRC government.

If United States dollar had strengthened/weakened by 5% against RMB with all other variables held constant, post-tax profit would have been RMB47,000, RMB308,000, RMB622,000, RMB554,000 and RMB723,000 higher/lower for the years ended 31 December 2012, 2013 and 2014 and four months ended 30 April 2014 and 2015, respectively, mainly as a result of foreign exchange gains or losses on translation of United States dollar denominated trade receivables and cash and cash equivalents.

*(b) Cash flow and fair value interest risk*

Other than deposits held in banks and other financial institutions, entrusted loans and available-for-sale debt instrument, Huahong does not have significant interest-bearing assets. As at 31 December 2012, 2013 and 2014 and 30 April 2015, the average rate on deposits held in banks and other financial institutions was approximately 2.25%, 2.48%, 2.36% and 1.36% per annum, respectively. As at 31 December 2014, the entrusted loan to related parties bears interest at 5.20% per annum. As at 31 December 2013 and 2014 and 30 April 2015, the average rates on available-for-sale debt instrument were approximately 4.70%, 4.97% and 5.00% per annum, respectively. Any change in the interest rate from time to time is not considered to have significant impact to Huahong's performance.

*(c) Credit risk*

Credit risk of Huahong arises from cash and cash equivalents, long-term and short-term deposits, restricted deposits, available-for-sale financial assets and trade and other receivables. The maximum exposure to credit risk at the balance sheet date is their carrying value. Huahong has policies and procedures in place to ensure they are made to counterparties with acceptable credit quality.

All Huahong's deposits with banks and other financial institutions and short-term deposits are placed in high quality financial institutions without significant exposure to credit risk.

For trade and other receivables, the credit quality of the counterparties is assessed by taking into account their financial position, credit history and other factors. Individual credit limits are set based on the assessment of the credit quality. Given the constant repayment history, the directors are of the opinion that the risk of default by these counterparties is not significant. Further disclosure on credit risk is set out in Note 14.

*(d) Liquidity risk*

Liquidity risk refers to the risk that funds will not be available to meet liabilities as they fall due, and results from timing and amount mismatches of cash inflow and outflow. Huahong manages liquidity risk by maintaining sufficient cash balances and bank deposits (which are readily convertible to known amounts of cash) to meet its funding needs, including working capital and dividend payments.

The table below analyses Huahong's financial liabilities by maturity groupings based on the remaining period at the balance sheet date to the contractual maturity date. The amounts disclosed in the table are based on the contractual undiscounted cash flows of the financial liabilities.

|                                                                                                                                    | On demand<br>RMB'000 | Within 1 year<br>RMB'000 |
|------------------------------------------------------------------------------------------------------------------------------------|----------------------|--------------------------|
| At 31 December 2012                                                                                                                |                      |                          |
| Trade and other payables<br>(excluding other taxes<br>payable and salary payable)<br>and amount due to ultimate<br>holding company | —                    | 186,942                  |
| At 31 December 2013                                                                                                                |                      |                          |
| Trade and other payables<br>(excluding other taxes<br>payable and salary payable)<br>and amount due to ultimate<br>holding company | 15,000               | 149,788                  |
| At 31 December 2014                                                                                                                |                      |                          |
| Trade and other payables<br>(excluding other taxes<br>payable and salary payable)<br>and amount due to ultimate<br>holding company | 15,000               | 194,916                  |
| At 30 April 2015                                                                                                                   |                      |                          |
| Trade and other payables<br>(excluding other taxes<br>payable and salary payable)<br>and amount due to ultimate<br>holding company | 15,000               | 199,382                  |

**3.2    *Capital risk management***

Huahong's objectives when managing capital are to safeguard the ability to continue as a going concern in order to provide returns for its owners and benefits for other stakeholders and to maintain an optimal capital structure to reduce the cost of capital.

Huahong monitors capital risk by regularly reviewing the capital structure. As a part of this review, the directors of Huahong consider the cost of capital and the risks associated with the paid-in capital. To manage capital risk, Huahong may seek additional funding from the owners, adjust the amount of dividends paid to its owners or return capital to its owners.

In the opinion of the directors of Huahong, Huahong's capital risk is not significant.

**3.3    *Fair value estimation***

Financial instruments measured at fair value are grouped into Levels 1 to 3, based on the degree to which the fair value is observable, as follows:

- Level 1 fair value measurements are those derived from quoted prices (unadjusted) in active market for identical assets or liabilities.
- Level 2 fair value measurements are those derived from inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices).
- Level 3 fair value measurements are those derived from valuation techniques that include inputs for the asset or liability that are not based on observable market data (unobservable inputs).

The financial assets that are measured at fair value during the Relevant Periods are as follows:

|                     | Level 1<br><i>RMB'000</i> | Level 2<br><i>RMB'000</i> | Level 3<br><i>RMB'000</i> | Total<br><i>RMB'000</i> |
|---------------------|---------------------------|---------------------------|---------------------------|-------------------------|
| At 31 December 2012 | <u>–</u>                  | <u>–</u>                  | <u>–</u>                  | <u>–</u>                |
| At 31 December 2013 | <u>–</u>                  | <u>–</u>                  | <u>50,225</u>             | <u>50,225</u>           |
| At 31 December 2014 | <u>–</u>                  | <u>–</u>                  | <u>51,334</u>             | <u>51,334</u>           |
| At 30 April 2015    | <u>–</u>                  | <u>–</u>                  | <u>–</u>                  | <u>–</u>                |

See Notes 15 for disclosures of the available-for-sale financial assets that are measured at fair value.

The fair value of the following financial assets and liabilities approximate their carrying amount:

- Trade and other receivables
- Restricted deposits
- Short-term deposits
- Cash and cash equivalents
- Amount due to ultimate holding company
- Advances from customers
- Trade and other payables

**4. Critical accounting estimates and judgements****4.1 *Income tax and deferred taxation***

Estimation and judgement is required in determining the amount of the provision for income tax. There are transactions and calculations for which the ultimate tax determination is uncertain during the ordinary course of business. Where the final tax outcome of these matters is different from the amounts that were initially recognised, such differences will impact on the income tax and deferred taxation provisions in the period in which such determination is made.

**4.2 *Impairment of trade and other receivables***

Management reviews its trade and other receivables for objective evidence of impairment. Significant financial difficulty of the debtor, probability that the debtor will enter bankruptcy or financial reorganisation, and default or delinquency in payments are considered as objective evidence that a receivable is impaired. In determining this, management makes judgments as to whether there is observable data indicating that there has been a significant change in the payment ability of the debtor, or whether there have been significant changes with adverse effect on the market and economic environment in which the debtor operates. Where there is objective evidence of impairment, management makes judgments as to whether an impairment loss should be recognised as an expense.

As at 31 December 2012, 2013 and 2014 and 30 April 2015, provisions for impairment of trade and other receivables of Huahong are RMB1,225,000, RMB1,128,000, RMB3,366,000 and RMB1,497,000, respectively.

## 5. Revenue and segment information

## (a) Revenue

| Analysis of revenue<br>by category     | Year ended 31 December |                |                | Four months ended<br>30 April |                |
|----------------------------------------|------------------------|----------------|----------------|-------------------------------|----------------|
|                                        | 2012                   | 2013           | 2014           | 2014                          | 2015           |
|                                        | RMB'000                | RMB'000        | RMB'000        | RMB'000                       | RMB'000        |
|                                        |                        |                |                | (Unaudited)                   |                |
| Sale of integrated<br>circuit products | 552,565                | 478,746        | 456,213        | 132,766                       | 145,967        |
| Others                                 | 40                     | 381            | 956            | –                             | 401            |
|                                        | <u>552,605</u>         | <u>479,127</u> | <u>457,169</u> | <u>132,766</u>                | <u>146,368</u> |

## (b) Segment information

The chief operating decision-maker has been identified as the board of directors of Huahong. The board of directors reviews Huahong's internal reporting in order to assess performance and allocate resources. Management has determined the operating segments based on these reports.

The directors of Huahong consider that Huahong's operations are operated and managed as a single segment. Accordingly, no segment information is presented.

Revenues of approximately RMB238,554,000, RMB179,764,000, RMB143,982,000, RMB31,943,620 and RMB61,731,456 for each of the years ended 31 December 2012, 2013 and 2014, and for the four months ended 30 April 2014 and 2015, respectively, were derived from two, one, one, one and two external customer(s) from which the transactions amounted to 10 per cent or more of Huahong's revenues.

Nearly 90% of Huahong's revenue is attributable to the market in the PRC and nearly 100% of Huahong's non-current assets are located in the PRC. No geographical information is therefore presented.

## 6. Other income and gains – net

|                                                               | Year ended 31 December |                |                | Four months ended<br>30 April |                |
|---------------------------------------------------------------|------------------------|----------------|----------------|-------------------------------|----------------|
|                                                               | 2012                   | 2013           | 2014           | 2014                          | 2015           |
|                                                               | <i>RMB'000</i>         | <i>RMB'000</i> | <i>RMB'000</i> | <i>RMB'000</i><br>(Unaudited) | <i>RMB'000</i> |
| Government grants<br>(Note 23)                                | 23,419                 | 47,172         | 63,802         | 1,169                         | 14,050         |
| Interest income on<br>entrusted loans                         | –                      | –              | 2,658          | –                             | –              |
| Interest income on<br>available-for-sale<br>financial assets  | –                      | 225            | 3,094          | 1,554                         | 803            |
| Interest income on<br>short-term and long-<br>term deposits   | 1,746                  | 4,853          | 3,263          | 1,158                         | 98             |
| Value-added tax refund                                        | –                      | 1,491          | 9,343          | 2,027                         | 847            |
| Interest income<br>on deferred<br>consideration<br>receivable | 1,354                  | –              | –              | –                             | –              |
| Others                                                        | 1,682                  | 1,349          | 552            | (85)                          | (584)          |
|                                                               | <u>28,201</u>          | <u>55,090</u>  | <u>82,712</u>  | <u>5,823</u>                  | <u>15,214</u>  |

## 7. Expenses by nature

Expenses included in cost of sales, selling and marketing costs and administrative expenses are analysed as follows:

|                                                                               | Year ended 31 December |                |                | Four months ended<br>30 April |                |
|-------------------------------------------------------------------------------|------------------------|----------------|----------------|-------------------------------|----------------|
|                                                                               | 2012                   | 2013           | 2014           | 2014                          | 2015           |
|                                                                               | RMB'000                | RMB'000        | RMB'000        | RMB'000<br>(Unaudited)        | RMB'000        |
| Employee benefit expenses ( <i>Note 8</i> )                                   | 68,724                 | 73,575         | 69,927         | 24,770                        | 23,371         |
| Depreciation expenses                                                         | 3,653                  | 5,175          | 6,513          | 2,205                         | 2,202          |
| Changes in inventories of finished goods and work in progress                 | 25,057                 | 15,421         | (26,061)       | (6,622)                       | (59,127)       |
| Impairment/(reversal of impairment) provision for trade and other receivables | 1,079                  | (97)           | 2,238          | 338                           | (1,869)        |
| Raw materials and consumables used                                            | 404,133                | 339,705        | 389,133        | 106,558                       | 186,170        |
| Operating lease expenses on properties                                        | 5,960                  | 6,343          | 6,112          | 1,823                         | 1,554          |
| Auditor's remuneration                                                        | 233                    | 136            | 286            | 88                            | 90             |
| Labor outsourcing expenses                                                    | 3,831                  | 4,669          | 7,210          | 2,031                         | 3,925          |
| Travel expense                                                                | 5,735                  | 5,645          | 7,302          | 1,930                         | 1,878          |
| Other expenses                                                                | 25,618                 | 23,978         | 28,079         | 13,263                        | 5,622          |
|                                                                               | <u>544,023</u>         | <u>474,550</u> | <u>490,739</u> | <u>146,384</u>                | <u>163,816</u> |

Research and development costs for each of the years ended 31 December 2012, 2013 and 2014, and for the four months ended 30 April 2014 and 2015 were approximately RMB96,855,000, RMB104,575,000, RMB114,557,000, RMB35,823,000 and RMB37,029,000, respectively. Research and development costs mainly comprised of employee costs of RMB45,891,000, RMB50,321,000, RMB40,475,000, RMB15,203,000 and RMB14,302,000 and material costs of RMB45,820,000, RMB47,277,000, RMB65,326,000, RMB18,168,000 and RMB19,750,000, for the years ended 31 December 2012, 2013 and 2014, and for the four months ended 30 April 2014 and 2015, respectively. No research and development costs were capitalised during the Relevant Periods.

## 8. Employee benefit expenses

|                                                      | Year ended 31 December |                |                | Four months ended<br>30 April |                |
|------------------------------------------------------|------------------------|----------------|----------------|-------------------------------|----------------|
|                                                      | 2012                   | 2013           | 2014           | 2014                          | 2015           |
|                                                      | <i>RMB'000</i>         | <i>RMB'000</i> | <i>RMB'000</i> | <i>RMB'000</i>                | <i>RMB'000</i> |
|                                                      |                        |                |                | (Unaudited)                   |                |
| Salaries, allowances<br>and benefits in kind         | 62,735                 | 66,831         | 63,252         | 22,525                        | 21,102         |
| Contributions to<br>retirement schemes<br>(Note (i)) | 5,989                  | 6,744          | 6,675          | 2,245                         | 2,269          |
|                                                      | <u>68,724</u>          | <u>73,575</u>  | <u>69,927</u>  | <u>24,770</u>                 | <u>23,371</u>  |

- (i) Huahong participates in defined contribution retirement scheme based on laws and regulations in the PRC. The local government authority of the PRC is responsible for the pension liabilities to these retired employees in the PRC. Huahong made contributions to retirement schemes in the PRC which are expensed as incurred.

**(a) Directors' and chief executive's emoluments**

The remuneration of each director and the chief executive of Huahong for the year ended 31 December 2012 is set out below (*Note (i)*):

|                                                       | Fees      | Salaries,<br>allowances<br>and benefits<br>in kind | Pension<br>scheme<br>contributions | Discret-<br>ionary<br>bonus | Others    | Total        |
|-------------------------------------------------------|-----------|----------------------------------------------------|------------------------------------|-----------------------------|-----------|--------------|
|                                                       | RMB'000   | RMB'000                                            | RMB'000                            | RMB'000                     | RMB'000   | RMB'000      |
| <b>Name of Director</b>                               |           |                                                    |                                    |                             |           |              |
| Mr. Zhao Guiwu                                        | 6         | 280                                                | 17                                 | 250                         | 17        | 570          |
| Mr. Li Rongxin ( <i>Chief<br/>Executive Officer</i> ) | –         | 523                                                | 33                                 | 250                         | 34        | 840          |
| Mr. Ma Yuchuan                                        | 8         | –                                                  | –                                  | –                           | –         | 8            |
| Mr. Chen Jianbo                                       | 8         | –                                                  | –                                  | –                           | –         | 8            |
| Mr. Yu Jun                                            | 2         | –                                                  | –                                  | –                           | –         | 2            |
| Mr. Li Zhaoming                                       | 6         | –                                                  | –                                  | –                           | –         | 6            |
| Mr. Chen Yonghong                                     | 6         | –                                                  | –                                  | –                           | –         | 6            |
| <b>Name of Supervisor</b>                             |           |                                                    |                                    |                             |           |              |
| Mr. Zhou Honghua                                      | 8         | –                                                  | –                                  | –                           | –         | 8            |
| Mr. Niu Xinwei                                        | 8         | –                                                  | –                                  | –                           | –         | 8            |
| Mr. Bao Sigang                                        | –         | 28                                                 | 3                                  | 10                          | 2         | 43           |
| Mr. Tian Tao                                          | –         | 266                                                | 31                                 | 59                          | 13        | 369          |
|                                                       | <u>52</u> | <u>1,097</u>                                       | <u>84</u>                          | <u>569</u>                  | <u>66</u> | <u>1,868</u> |

The remuneration of each director and the chief executive of Huahong for the year ended 31 December 2013 is set out below (*Note (ii)*):

| Name of Director                                      | Fees    | Salaries,<br>allowances<br>and benefits | Pension<br>scheme<br>contributions | Discret-<br>ionary<br>bonus | Others  | Total   |
|-------------------------------------------------------|---------|-----------------------------------------|------------------------------------|-----------------------------|---------|---------|
|                                                       | RMB'000 | RMB'000                                 | RMB'000                            | RMB'000                     | RMB'000 | RMB'000 |
| Mr. Zhao Guiwu                                        | –       | 571                                     | 36                                 | 250                         | 34      | 891     |
| Mr. Li Rongxin ( <i>Chief<br/>Executive Officer</i> ) | –       | 518                                     | 36                                 | 250                         | 34      | 838     |
| Mr. Yu Jun                                            | 2       | –                                       | –                                  | –                           | –       | 2       |
| Mr. Ma Yuchuan                                        | 2       | –                                       | –                                  | –                           | –       | 2       |
| Mr. Xiang Xiang                                       | 2       | –                                       | –                                  | –                           | –       | 2       |
| Mr. Chen Jianbo                                       | 2       | –                                       | –                                  | –                           | –       | 2       |
| <b>Name of Supervisor</b>                             |         |                                         |                                    |                             |         |         |
| Mr. Zhou Honghua                                      | 2       | –                                       | –                                  | –                           | –       | 2       |
| Mr. Bao Sigang                                        | –       | 378                                     | 36                                 | 134                         | 18      | 566     |
| Mr. Niu Xinwei                                        | 2       | –                                       | –                                  | –                           | –       | 2       |
|                                                       | 12      | 1,467                                   | 108                                | 634                         | 86      | 2,307   |

The remuneration of each director and the chief executive of Huahong for the year ended 31 December 2014 is set out below (*Note (iii)*):

| Name of Director                                      | Fees    | Salaries,<br>allowances<br>and<br>benefits<br>in kind | Pension<br>scheme<br>contributions | Discret-<br>ionary<br>bonus | Others  | Total   |
|-------------------------------------------------------|---------|-------------------------------------------------------|------------------------------------|-----------------------------|---------|---------|
|                                                       | RMB'000 | RMB'000                                               | RMB'000                            | RMB'000                     | RMB'000 | RMB'000 |
| Mr. Zhao Guiwu                                        | –       | 472                                                   | 33                                 | 286                         | 35      | 826     |
| Mr. Dong Haoran                                       | –       | –                                                     | –                                  | –                           | –       | –       |
| Mr. Li Rongxin ( <i>Chief<br/>Executive Officer</i> ) | –       | 573                                                   | 37                                 | 344                         | 44      | 998     |
| Mr. Yu Jun                                            | 2       | –                                                     | –                                  | –                           | –       | 2       |
| Mr. Ma Yuchuan                                        | 2       | –                                                     | –                                  | –                           | –       | 2       |
| Mr. Xiang Xiang                                       | 2       | –                                                     | –                                  | –                           | –       | 2       |
| Mr. Wang Liqiang                                      | –       | –                                                     | –                                  | –                           | –       | –       |
| <b>Name of Supervisor</b>                             |         |                                                       |                                    |                             |         |         |
| Mr. Bao Sigang                                        | –       | 366                                                   | 37                                 | 123                         | 33      | 559     |
| Mr. Jiang Juncheng                                    | –       | –                                                     | –                                  | –                           | –       | –       |
| Mr. Niu Xinwei                                        | 2       | –                                                     | –                                  | –                           | –       | 2       |
| Mr. Zhou Honghua                                      | 2       | –                                                     | –                                  | –                           | –       | 2       |
|                                                       | 10      | 1,411                                                 | 107                                | 753                         | 112     | 2,393   |

The unaudited remuneration of each director and the chief executive of Huahong for the four months ended 30 April 2014 is set out below:

| Name of Director                                      | Salaries,<br>allowances<br>and<br>benefits<br>in kind |     |                                                      |                                               |                          | Total |
|-------------------------------------------------------|-------------------------------------------------------|-----|------------------------------------------------------|-----------------------------------------------|--------------------------|-------|
|                                                       | Fees<br><i>RMB'000</i>                                |     | Pension<br>scheme<br>contributions<br><i>RMB'000</i> | Discret-<br>ionary<br>bonus<br><i>RMB'000</i> | Others<br><i>RMB'000</i> |       |
| Mr. Zhao Guiwu                                        | –                                                     | 188 | 13                                                   | 95                                            | 11                       | 307   |
| Mr. Li Rongxin ( <i>Chief<br/>Executive Officer</i> ) | –                                                     | 190 | 12                                                   | 115                                           | 11                       | 328   |
| Mr. Yu Jun                                            | 2                                                     | –   | –                                                    | –                                             | –                        | 2     |
| Mr. Ma Yuchuan                                        | 2                                                     | –   | –                                                    | –                                             | –                        | 2     |
| Mr. Xiang Xiang                                       | 2                                                     | –   | –                                                    | –                                             | –                        | 2     |
| <b>Name of Supervisor</b>                             |                                                       |     |                                                      |                                               |                          |       |
| Mr. Bao Sigang                                        | –                                                     | 129 | 12                                                   | 41                                            | 7                        | 189   |
| Mr. Zhou Honghua                                      | 2                                                     | –   | –                                                    | –                                             | –                        | 2     |
| Mr. Niu Xinwei                                        | 2                                                     | –   | –                                                    | –                                             | –                        | 2     |
|                                                       | 10                                                    | 507 | 37                                                   | 251                                           | 29                       | 834   |

The remuneration of each director and the chief executive of Huahong for the four months ended 30 April 2015 is set out below (*Note (iv)*):

| Name of Director                                      | Fees     | Salaries,<br>allowances<br>and<br>benefits<br>in kind | Pension<br>scheme<br>contributions | Discret-<br>ionary<br>bonus | Others    | Total      |
|-------------------------------------------------------|----------|-------------------------------------------------------|------------------------------------|-----------------------------|-----------|------------|
|                                                       | RMB'000  | RMB'000                                               | RMB'000                            | RMB'000                     | RMB'000   | RMB'000    |
| Mr. Dong Haoran                                       | -        | -                                                     | -                                  | -                           | -         | -          |
| Mr. Li Rongxin ( <i>Chief<br/>Executive Officer</i> ) | -        | -                                                     | -                                  | -                           | -         | -          |
| Mr. Ma Yuchuan                                        | -        | -                                                     | -                                  | -                           | -         | -          |
| Mr. Xiang Xiang                                       | -        | -                                                     | -                                  | -                           | -         | -          |
| Mr. Wang Liqiang                                      | -        | -                                                     | -                                  | -                           | -         | -          |
| <b>Name of Supervisor</b>                             |          |                                                       |                                    |                             |           |            |
| Mr. Bao Sigang                                        | -        | 118                                                   | 13                                 | -                           | 14        | 145        |
| Mr. Jiang Juncheng                                    | -        | -                                                     | -                                  | -                           | -         | -          |
|                                                       | <u>-</u> | <u>118</u>                                            | <u>13</u>                          | <u>-</u>                    | <u>14</u> | <u>145</u> |

- (i) During the year ended 31 December 2012, Mr. Li Zhaoming and Mr. Chen Yonghong resigned from their position as directors; Mr. Yu Jun was appointed as director. Mr. Tian Tao resigned from his position as supervisor; Mr. Bao Sigang was appointed as supervisor.
- (ii) During the year ended 31 December 2013, Mr. Chen Jianbo resigned from his position as director; Mr. Xiang Xiang was appointed as director.
- (iii) During the year ended 31 December 2014, Mr. Zhao Guiwu and Mr. Yu Jun resigned from their position as directors; Mr. Zhou Honghua and Mr. Niu Xinwei resigned from their position as supervisors. Mr. Dong Haoran and Mr. Wang Liqiang were appointed as directors. Mr. Jiang Juncheng was appointed as supervisor.
- (iv) During the four months ended 30 April 2015, there was no change in directorship.

During the year ended 31 December 2012, 2013 and 2014 and the four months ended 30 April 2014, except for Mr. Li Rongxin, Mr. Zhao Guiwu, Mr. Tian Tao and Mr. Bao Sigang, the other directors and supervisors of Huahong received emoluments from CEC and its other subsidiaries.

During the four months ended 30 April 2015, except for Mr. Bao Sigang, the other directors of Huahong received emoluments from CEC and its other subsidiaries.

No directors received any emoluments from Huahong as an inducement to join or upon joining Huahong or as compensation for loss of office during the Relevant Periods.

**(b) Five highest paid individuals**

The five individuals whose emoluments were the highest in Huahong for each of the years ended 31 December 2012, 2013 and 2014 and the four months ended 30 April 2014 and 2015 included one, two, two, two and zero director(s) respectively. The emoluments paid and payable to the remaining four, three, three, three and five individuals for each of the years ended 31 December 2012, 2013 and 2014 and the four months ended 30 April 2014 and 2015, respectively are as follows:

|                                           | Year ended 31 December |              |              | Four months ended |            |
|-------------------------------------------|------------------------|--------------|--------------|-------------------|------------|
|                                           | 2012                   | 2013         | 2014         | 30 April 2014     | 2015       |
|                                           | RMB'000                | RMB'000      | RMB'000      | RMB'000           | RMB'000    |
|                                           |                        |              |              | (Unaudited)       |            |
| Salaries, allowances and benefits in kind | 1,722                  | 1,326        | 1,346        | 420               | 767        |
| Bonuses                                   | 1,012                  | 506          | 631          | 231               | –          |
| Contributions to retirement schemes       | 134                    | 108          | 112          | 36                | 65         |
|                                           | <u>2,868</u>           | <u>1,940</u> | <u>2,089</u> | <u>687</u>        | <u>832</u> |

Their emoluments fell within the following band:

|                    | Year ended 31 December |          |          | Four months ended |          |
|--------------------|------------------------|----------|----------|-------------------|----------|
|                    | 2012                   | 2013     | 2014     | 30 April 2014     | 2015     |
|                    |                        |          |          | (Unaudited)       |          |
| Nil – HKD1,000,000 | <u>4</u>               | <u>3</u> | <u>3</u> | <u>3</u>          | <u>5</u> |

**9. Finance income**

|                                                 | Year ended 31 December |         |         | Four months ended<br>30 April |         |
|-------------------------------------------------|------------------------|---------|---------|-------------------------------|---------|
|                                                 | 2012                   | 2013    | 2014    | 2014                          | 2015    |
|                                                 | RMB'000                | RMB'000 | RMB'000 | RMB'000                       | RMB'000 |
|                                                 |                        |         |         | (Unaudited)                   |         |
| Interest income on cash<br>and cash equivalents | 3,647                  | 4,571   | 2,105   | 774                           | 446     |

**10. Taxation**

|                                             | Year ended 31 December |         |         | Four months ended<br>30 April |         |
|---------------------------------------------|------------------------|---------|---------|-------------------------------|---------|
|                                             | 2012                   | 2013    | 2014    | 2014                          | 2015    |
|                                             | RMB'000                | RMB'000 | RMB'000 | RMB'000                       | RMB'000 |
|                                             |                        |         |         | (Unaudited)                   |         |
| Current taxation:                           |                        |         |         |                               |         |
| – PRC corporate<br>income tax<br>(Note (i)) | 3,990                  | –       | (4,269) | (4,269)                       | –       |
| Deferred taxation:                          |                        |         |         |                               |         |
| – PRC corporate<br>income tax               | 1,355                  | –       | –       | –                             | –       |
|                                             | 5,345                  | –       | (4,269) | (4,269)                       | –       |

- (i) In accordance with the corporate income tax laws of the PRC, the applicable statutory tax rate of Huahong is 25% from 1 January 2008. However, Huahong was qualified as an “Integrated Circuit Design Enterprises in National Planning Layout” (“ICDE”) and thus enjoyed a 10% preferential tax rate of corporate income tax from 1 January 2011 to 31 December 2014. Huahong was also qualified as “High and New Technology Enterprises” and enjoyed a 15% preferential tax rate of corporate income tax from 1 January 2015 to 31 December 2017.

- (a) Reconciliation between the taxation on Huahong's profit/(loss) before taxation and the theoretical taxation that would arise using the respective applicable tax rates are as follows:

|                                                                                               | Year ended 31 December |          |          | Four months ended |         |
|-----------------------------------------------------------------------------------------------|------------------------|----------|----------|-------------------|---------|
|                                                                                               | 2012                   | 2013     | 2014     | 30 April          | 2015    |
|                                                                                               | RMB'000                | RMB'000  | RMB'000  | RMB'000           | RMB'000 |
|                                                                                               |                        |          |          | (Unaudited)       |         |
| Profit/(loss) before taxation                                                                 | 40,430                 | 64,238   | 51,800   | (7,021)           | (2,261) |
| Tax calculated at PRC corporate income tax rate of 25%                                        | 10,108                 | 16,060   | 12,950   | (1,755)           | (565)   |
| Effect of tax concession                                                                      | (8,017)                | –        | –        | –                 | –       |
| Expenses not deductible for taxation purposes                                                 | 344                    | 449      | 444      | 111               | 222     |
| Research and development costs additional deductions                                          | (11,448)               | (12,355) | (12,012) | –                 | –       |
| Refunded taxation                                                                             | –                      | –        | (4,269)  | (4,269)           | –       |
| Temporary differences for which no deferred tax asset was recognised                          | 14,358                 | 213      | 1,924    | 264               | 1,237   |
| Utilisation of temporary differences for which deferred tax asset was previously unrecognised | –                      | (11,285) | (15,877) | (8,062)           | (6,620) |
| Tax losses for which no deferred tax asset was recognised                                     | –                      | 6,918    | 12,571   | 9,442             | 5,726   |
| Taxation                                                                                      | 5,345                  | –        | (4,269)  | (4,269)           | –       |

## (b) Deferred taxation

The movement in the deferred tax assets during the year of 2012 is as follows:

|                                     | Impairment<br>of inventories<br><i>RMB'000</i> | Impairment<br>of intangible<br>assets<br><i>RMB'000</i> | Accrued<br>expenses<br><i>RMB'000</i> | Total<br><i>RMB'000</i> |
|-------------------------------------|------------------------------------------------|---------------------------------------------------------|---------------------------------------|-------------------------|
| At 1 January 2012                   | 1,105                                          | 210                                                     | 40                                    | 1,355                   |
| Credited to the income<br>statement | <u>(1,105)</u>                                 | <u>(210)</u>                                            | <u>(40)</u>                           | <u>(1,355)</u>          |
| At 31 December 2012                 | <u><u>-</u></u>                                | <u><u>-</u></u>                                         | <u><u>-</u></u>                       | <u><u>-</u></u>         |

Deferred tax assets are recognised for tax losses carrying-forwards to the extent that the realisation of the related tax benefit through the future taxable profits is probable. Considering Huahong can continuously obtains the research and development cost additional deductions on the corporate income tax, the management estimated that Huahong would not generate taxable profit in future, as a result, Huahong did not recognise any deferred tax asset since the year ended 31 December 2012. For each of the years ended 31 December 2013 and 2014 and the four months ended 30 April 2014 and 2015, Huahong did not recognise deferred tax assets in respect of tax losses amounting to RMB27,670,000, RMB77,957,000, RMB65,440,000 and RMB128,533,000 which expire in 2018, 2019, and 2020 respectively. Also for each of the years ended 31 December 2012, 2013 and 2014 and the four months ended 30 April 2014 and 2015, Huahong did not recognise deferred tax assets in respect of temporary deductible differences amounting to RMB224,037,000, RMB179,751,000, RMB123,938,000, RMB148,560,000 and RMB102,407,000, respectively.

## 11. Property, plant and equipment

|                                    | Buildings<br>and<br>leasehold<br>improvements<br><i>RMB'000</i> | Plant and<br>machinery<br><i>RMB'000</i> | Motor<br>vehicles<br><i>RMB'000</i> | Furniture<br>and fixtures<br><i>RMB'000</i> | Total<br><i>RMB'000</i> |
|------------------------------------|-----------------------------------------------------------------|------------------------------------------|-------------------------------------|---------------------------------------------|-------------------------|
| <b>At 1 January 2012</b>           |                                                                 |                                          |                                     |                                             |                         |
| Cost                               | 887                                                             | 40,833                                   | 1,214                               | 2,665                                       | 45,599                  |
| Accumulated depreciation           | (15)                                                            | (31,994)                                 | (268)                               | (2,170)                                     | (34,447)                |
| Net book amount                    | 872                                                             | 8,839                                    | 946                                 | 495                                         | 11,152                  |
| <b>Year ended 31 December 2012</b> |                                                                 |                                          |                                     |                                             |                         |
| Opening net book amount            | 872                                                             | 8,839                                    | 946                                 | 495                                         | 11,152                  |
| Additions                          | 100                                                             | 4,638                                    | –                                   | 257                                         | 4,995                   |
| Disposals                          | –                                                               | (23)                                     | –                                   | (63)                                        | (86)                    |
| Depreciation                       | (179)                                                           | (3,124)                                  | (233)                               | (117)                                       | (3,653)                 |
| Closing net book amount            | 793                                                             | 10,330                                   | 713                                 | 572                                         | 12,408                  |
| <b>At 31 December 2012</b>         |                                                                 |                                          |                                     |                                             |                         |
| Cost                               | 987                                                             | 45,023                                   | 1,214                               | 2,858                                       | 50,082                  |
| Accumulated depreciation           | (194)                                                           | (34,693)                                 | (501)                               | (2,286)                                     | (37,674)                |
| Net book amount                    | 793                                                             | 10,330                                   | 713                                 | 572                                         | 12,408                  |
| <b>Year ended 31 December 2013</b> |                                                                 |                                          |                                     |                                             |                         |
| Opening net book amount            | 793                                                             | 10,330                                   | 713                                 | 572                                         | 12,408                  |
| Additions                          | 31,141                                                          | 4,521                                    | –                                   | 678                                         | 36,340                  |
| Disposals                          | (55)                                                            | (273)                                    | –                                   | (9)                                         | (337)                   |
| Depreciation                       | (1,197)                                                         | (3,572)                                  | (233)                               | (173)                                       | (5,175)                 |
| Closing net book amount            | 30,682                                                          | 11,006                                   | 480                                 | 1,068                                       | 43,236                  |
| <b>At 31 December 2013</b>         |                                                                 |                                          |                                     |                                             |                         |
| Cost                               | 32,073                                                          | 42,726                                   | 1,214                               | 3,523                                       | 79,536                  |
| Accumulated depreciation           | (1,391)                                                         | (31,720)                                 | (734)                               | (2,455)                                     | (36,300)                |
| Net book amount                    | 30,682                                                          | 11,006                                   | 480                                 | 1,068                                       | 43,236                  |

|                                    | Buildings<br>and<br>leasehold<br>improvements<br><i>RMB'000</i> | Plant and<br>machinery<br><i>RMB'000</i> | Motor<br>vehicles<br><i>RMB'000</i> | Furniture<br>and fixtures<br><i>RMB'000</i> | Total<br><i>RMB'000</i> |
|------------------------------------|-----------------------------------------------------------------|------------------------------------------|-------------------------------------|---------------------------------------------|-------------------------|
| <b>Year ended 31 December 2014</b> |                                                                 |                                          |                                     |                                             |                         |
| Opening net book amount            | 30,682                                                          | 11,006                                   | 480                                 | 1,068                                       | 43,236                  |
| Additions                          | 920                                                             | 5,021                                    | –                                   | 244                                         | 6,185                   |
| Disposals                          | –                                                               | (384)                                    | –                                   | (3)                                         | (387)                   |
| Depreciation                       | (2,037)                                                         | (3,971)                                  | (212)                               | (293)                                       | (6,513)                 |
| Closing net book amount            | <u>29,565</u>                                                   | <u>11,672</u>                            | <u>268</u>                          | <u>1,016</u>                                | <u>42,521</u>           |
| <b>At 31 December 2014</b>         |                                                                 |                                          |                                     |                                             |                         |
| Cost                               | 32,993                                                          | 47,034                                   | 1,214                               | 3,727                                       | 84,968                  |
| Accumulated depreciation           | <u>(3,428)</u>                                                  | <u>(35,362)</u>                          | <u>(946)</u>                        | <u>(2,711)</u>                              | <u>(42,447)</u>         |
| Net book amount                    | <u>29,565</u>                                                   | <u>11,672</u>                            | <u>268</u>                          | <u>1,016</u>                                | <u>42,521</u>           |
| <b>Period ended 30 April 2015</b>  |                                                                 |                                          |                                     |                                             |                         |
| Opening net book amount            | 29,565                                                          | 11,672                                   | 268                                 | 1,016                                       | 42,521                  |
| Additions                          | 196                                                             | 3,034                                    | –                                   | 197                                         | 3,427                   |
| Depreciation                       | <u>(693)</u>                                                    | <u>(1,332)</u>                           | <u>(66)</u>                         | <u>(111)</u>                                | <u>(2,202)</u>          |
| Closing net book amount            | <u>29,068</u>                                                   | <u>13,374</u>                            | <u>202</u>                          | <u>1,102</u>                                | <u>43,746</u>           |
| <b>At 30 April 2015</b>            |                                                                 |                                          |                                     |                                             |                         |
| Cost                               | 33,190                                                          | 50,063                                   | 1,213                               | 3,924                                       | 88,390                  |
| Accumulated depreciation           | <u>(4,122)</u>                                                  | <u>(36,689)</u>                          | <u>(1,011)</u>                      | <u>(2,822)</u>                              | <u>(44,644)</u>         |
| Net book amount                    | <u>29,068</u>                                                   | <u>13,374</u>                            | <u>202</u>                          | <u>1,102</u>                                | <u>43,746</u>           |

For each of the years ended 31 December 2012, 2013 and 2014 and the four months ended 30 April 2014 and 2015, depreciation expense charged to administrative expenses, cost of sales and selling and marketing costs, respectively, are as follows:

|                             | Year ended 31 December |                |                | Four months ended<br>30 April |                |
|-----------------------------|------------------------|----------------|----------------|-------------------------------|----------------|
|                             | 2012                   | 2013           | 2014           | 2014                          | 2015           |
|                             | <i>RMB'000</i>         | <i>RMB'000</i> | <i>RMB'000</i> | <i>RMB'000</i>                | <i>RMB'000</i> |
|                             |                        |                |                | (Unaudited)                   |                |
| Administrative expenses     | 3,208                  | 4,498          | 5,840          | 1,969                         | 1,994          |
| Cost of sales               | 375                    | 599            | 612            | 23                            | 18             |
| Selling and marketing costs | 70                     | 78             | 61             | 213                           | 190            |
|                             | <u>3,653</u>           | <u>5,175</u>   | <u>6,513</u>   | <u>2,205</u>                  | <u>2,202</u>   |

For each of the years ended 31 December 2012, 2013 and 2014 and the four months ended 30 April 2014 and 2015, lease rental expenses amounting to RMB5,960,000, RMB6,343,000, RMB6,112,000, RMB1,823,000 and RMB1,554,000 relating to the lease of certain properties for office use are included in profit or loss.

**12. Investment in a joint venture**

|                              | Year ended<br>31 December<br>2014<br><i>RMB'000</i> | Four months<br>ended 30 April<br>2015<br><i>RMB'000</i> |
|------------------------------|-----------------------------------------------------|---------------------------------------------------------|
| Beginning of the year/period | –                                                   | 5,653                                                   |
| Capital contribution         | 5,100                                               | –                                                       |
| Share of profit/(loss)       | <u>553</u>                                          | <u>(473)</u>                                            |
| End of the year/period       | <u>5,653</u>                                        | <u>5,180</u>                                            |

In 2014, Huahong together with Chongqing Expressway Group Co., Ltd (重慶高速公路集團有限公司) established Chongqing Huahong Electronics Co., Ltd (重慶華虹電子有限公司, “Chongqing Huahong”). Huahong contributed RMB5,100,000 in cash, which represents 51% of the registered capital of Chongqing Huahong.

Pursuant to the articles of association of Chongqing Huahong, all key operating and financial decisions shall be approved by both venturers. Therefore, Chongqing Huahong is accounted for as a joint venture of Huahong.

Particulars of joint venture at 31 December 2014 and 30 April 2015 are as follows:

| Name              | Place of establishment and type of legal entity | Principal place of operation and activities      | Registered and paid-in capital | Interest held |
|-------------------|-------------------------------------------------|--------------------------------------------------|--------------------------------|---------------|
| Chongqing Huahong | PRC, limited liability company                  | PRC, design and sale of integrated circuit chips | RMB10,000,000                  | 51%           |

As at 31 December 2014 and 30 April 2015, in the opinion of the directors, the joint venture, Chongqing Huahong, is not material to Huahong, and thus the financial information of Chongqing Huahong is not disclosed.

### 13. Inventories

|                                | As at 31 December |                 |                 | As at           |
|--------------------------------|-------------------|-----------------|-----------------|-----------------|
|                                | 2012              | 2013            | 2014            | 30 April        |
|                                | RMB'000           | RMB'000         | RMB'000         | RMB'000         |
| Work in progress               | 32,225            | 15,122          | 20,305          | 48,536          |
| Finished goods                 | 88,816            | 77,178          | 92,842          | 126,952         |
|                                | <u>121,041</u>    | <u>92,300</u>   | <u>113,147</u>  | <u>175,488</u>  |
| Less: provision of inventories | <u>(33,775)</u>   | <u>(20,455)</u> | <u>(15,241)</u> | <u>(18,455)</u> |
|                                | <u>87,266</u>     | <u>71,845</u>   | <u>97,906</u>   | <u>157,033</u>  |

For each of the years ended 31 December 2012, 2013 and 2014 and the four months ended 30 April 2014, the cost of inventories recognised in cost of sales amounted to RMB383,370,000, RMB307,849,000, RMB297,747,000 and RMB87,845,000, respectively.

For the four months ended 30 April 2015, the cost of inventories recognised in cost of sales amounted to RMB109,027,000, which included write-down of inventory of RMB3,214,000.

#### 14. Trade and other receivables

|                                                        | As at 31 December |                |                | As at<br>30 April |
|--------------------------------------------------------|-------------------|----------------|----------------|-------------------|
|                                                        | 2012              | 2013           | 2014           | 2015              |
|                                                        | RMB'000           | RMB'000        | RMB'000        | RMB'000           |
| Trade receivables                                      | 256,458           | 218,393        | 212,621        | 272,166           |
| Less: provisions for<br>impairment ( <i>Note (c)</i> ) | (1,203)           | (909)          | (3,097)        | (1,297)           |
| Trade receivables – net                                | 255,255           | 217,484        | 209,524        | 270,869           |
| Prepayments and deposits                               | 6,629             | 13,333         | 20,772         | 10,486            |
| Other receivables                                      | 1,886             | 3,030          | 3,849          | 1,585             |
| Interest receivables                                   | 1,372             | 2,059          | 101            | 90                |
| Others                                                 | 3,944             | –              | 2,122          | 5,262             |
|                                                        | <u>269,086</u>    | <u>235,906</u> | <u>236,368</u> | <u>288,292</u>    |

As at 31 December 2012, 2013 and 2014 and 30 April 2015, the carrying amounts of trade and other receivables of Huahong approximate their fair values considering the collection of trade and other receivable is expected in one year or less.

Trade and other receivables of Huahong at 31 December 2012, 2013 and 2014 and 30 April 2015 are denominated in the following currencies:

|                       | As at 31 December |                |                | As at<br>30 April |
|-----------------------|-------------------|----------------|----------------|-------------------|
|                       | 2012              | 2013           | 2014           | 2015              |
|                       | RMB'000           | RMB'000        | RMB'000        | RMB'000           |
| RMB                   | 268,086           | 224,680        | 225,621        | 278,500           |
| United States dollars | 1,000             | 11,226         | 10,747         | 9,792             |
|                       | <u>269,086</u>    | <u>235,906</u> | <u>236,368</u> | <u>288,292</u>    |

- (a) The major of Huahong's sales are with credit terms of 10 days to 180 days. The remaining amounts are due immediately after the delivery of goods. As at 31 December 2012, 2013 and 2014 and 30 April 2015, the ageing analysis of the trade receivables based on invoice date are as follows:

|                                   | As at 31 December |                |                | As at<br>30 April |
|-----------------------------------|-------------------|----------------|----------------|-------------------|
|                                   | 2012              | 2013           | 2014           | 2015              |
|                                   | RMB'000           | RMB'000        | RMB'000        | RMB'000           |
| Current to 30 days                | 71,114            | 69,674         | 94,727         | 45,152            |
| 31 – 60 days                      | 33,200            | 25,996         | 38,246         | 55,947            |
| Over 60 days and<br>within 1 year | 144,459           | 118,798        | 70,563         | 164,008           |
| Over 1 year                       | <u>7,685</u>      | <u>3,925</u>   | <u>9,085</u>   | <u>7,059</u>      |
|                                   | <u>256,458</u>    | <u>218,393</u> | <u>212,621</u> | <u>272,166</u>    |

- (b) Trade receivables which were past due but not impaired related to a number of customers with high reputation for whom there is no recent history of default, the over due ageing analysis of these trade receivables are as follows:

|                                   | As at 31 December |                |               | As at<br>30 April |
|-----------------------------------|-------------------|----------------|---------------|-------------------|
|                                   | 2012              | 2013           | 2014          | 2015              |
|                                   | RMB'000           | RMB'000        | RMB'000       | RMB'000           |
| Within 30 days                    | 55,197            | 49,518         | 25,427        | 24,595            |
| 31 – 60 days                      | 27,909            | 32,695         | 14,390        | 20,539            |
| Over 60 days and<br>within 1 year | 45,943            | 29,986         | 26,817        | 85,098            |
| Over 1 year                       | <u>604</u>        | <u>3,015</u>   | <u>2,134</u>  | <u>5,762</u>      |
|                                   | <u>129,653</u>    | <u>115,214</u> | <u>68,768</u> | <u>135,994</u>    |

- (c) The individually impaired trade receivables mainly related to certain customers which were in unexpectedly difficult economic situations. It was assessed that these receivables were not expected to be recovered and thus full impairment provision was provided against them.

Movements in the provision for impairment on Huahong's trade receivables are as follows:

|                                                   | As at 31 December |                |                | As at<br>30 April |
|---------------------------------------------------|-------------------|----------------|----------------|-------------------|
|                                                   | 2012              | 2013           | 2014           | 2015              |
|                                                   | <i>RMB'000</i>    | <i>RMB'000</i> | <i>RMB'000</i> | <i>RMB'000</i>    |
| Beginning of the year/period                      | 145               | 1,203          | 909            | 3,097             |
| Impairment provision/<br>(Reversal of impairment) | 1,058             | (294)          | 2,188          | (1,800)           |
| End of the year/period                            | <u>1,203</u>      | <u>909</u>     | <u>3,097</u>   | <u>1,297</u>      |

#### 15. Available-for-sale financial assets

|                              | As at 31 December |                |                | As at<br>30 April |
|------------------------------|-------------------|----------------|----------------|-------------------|
|                              | 2012              | 2013           | 2014           | 2015              |
|                              | <i>RMB'000</i>    | <i>RMB'000</i> | <i>RMB'000</i> | <i>RMB'000</i>    |
| Beginning of the year/period | –                 | –              | 50,225         | 51,334            |
| Additions                    | –                 | 50,225         | 209,824        | –                 |
| Disposals                    | –                 | –              | (208,715)      | (51,334)          |
| End of the year/period       | <u>–</u>          | <u>50,225</u>  | <u>51,334</u>  | <u>–</u>          |

The available-for-sale financial assets represent investments in wealth management products issued by state-owned banks in the PRC with expected return range from 4.7% to 5.0% per annum and will mature within one year. As at 31 December 2012, 2013 and 2014 and 30 April 2015, the fair value approximated the carrying amount. The fair values are based on cash flow discounted using the expected return based on management judgment and are within level 3 of the fair value hierarchy.

The maximum exposure to credit risk is the carrying value of the wealth management products classified as available-for-sale. The fair value of the embedded derivative included in the available-for-sale financial assets is insignificant.

None of these available-for-sale financial assets is either past due or impaired.

#### 16. Restricted deposits

|                                 | As at 31 December |            |              | As at<br>30 April |
|---------------------------------|-------------------|------------|--------------|-------------------|
|                                 | 2012              | 2013       | 2014         | 2015              |
|                                 | RMB'000           | RMB'000    | RMB'000      | RMB'000           |
| At banks                        | 4,579             | 225        | 225          | –                 |
| At other financial institutions |                   |            |              |                   |
| – A related party (Note 27)     | –                 | –          | 1,976        | –                 |
|                                 | <u>4,579</u>      | <u>225</u> | <u>2,201</u> | <u>–</u>          |

Restricted deposits which are denominated in RMB represent guaranteed deposits for notes payables.

#### 17. Short-term and long-term deposits

|                                 | As at 31 December |                |              | As at<br>30 April |
|---------------------------------|-------------------|----------------|--------------|-------------------|
|                                 | 2012              | 2013           | 2014         | 2015              |
|                                 | RMB'000           | RMB'000        | RMB'000      | RMB'000           |
| Short-term deposits (Note (a))  |                   |                |              |                   |
| At banks                        | 35,064            | 50,254         | –            | –                 |
| At other financial institutions |                   |                |              |                   |
| – A related party (Note 27)     | 41,000            | 53,000         | 1,000        | 1,000             |
|                                 | <u>76,064</u>     | <u>103,254</u> | <u>1,000</u> | <u>1,000</u>      |
| Long-term deposits (Note (a))   |                   |                |              |                   |
| At banks                        | 10,000            | –              | –            | –                 |
|                                 | <u>86,064</u>     | <u>103,254</u> | <u>1,000</u> | <u>1,000</u>      |

- (a) Short-term deposits represent deposits at banks and other financial institutions with original maturity over 3 months and within 1 year. Long-term deposits represent deposits at banks with maturity over 1 year. As at 31 December 2012, 2013 and 2014 and 30 April 2015, the effective interest rates on short-term and long-term deposits were 3.00%, 3.14%, 3.30% and 3.30% per annum, respectively.

# 18. Cash and cash equivalents

|                                 | As at 31 December     |                       |                       | As at<br>30 April     |
|---------------------------------|-----------------------|-----------------------|-----------------------|-----------------------|
|                                 | 2012                  | 2013                  | 2014                  | 2015                  |
|                                 | RMB'000               | RMB'000               | RMB'000               | RMB'000               |
| Cash                            |                       |                       |                       |                       |
| At banks and on hand            | 94,613                | 151,238               | 105,169               | 92,282                |
| At other financial institutions |                       |                       |                       |                       |
| – A related party (Note 27)     | 224,374               | 51,499                | 89,852                | 22,056                |
|                                 | <u>318,987</u>        | <u>202,737</u>        | <u>195,021</u>        | <u>114,338</u>        |
| Short-term deposits (Note (a))  |                       |                       |                       |                       |
| At banks                        | 10,000                | 10,000                | –                     | –                     |
| At other financial institutions |                       |                       |                       |                       |
| – A related party (Note 27)     | 50,000                | 80,000                | 20,000                | 20,000                |
|                                 | <u>60,000</u>         | <u>90,000</u>         | <u>20,000</u>         | <u>20,000</u>         |
|                                 | <u><u>378,987</u></u> | <u><u>292,737</u></u> | <u><u>215,021</u></u> | <u><u>134,338</u></u> |

- (a) Short-term deposits represent deposits at banks and other financial institutions with original maturity of 3 months or less. As at 31 December 2012, 2013 and 2014 and 30 April 2015, the effective interest rates on short-term deposits were 2.82%, 2.88%, 2.82% and 2.73% per annum, respectively.

As at 31 December 2012, 2013 and 2014 and 30 April 2015, cash and cash equivalents of Huahong are denominated in the following currencies:

|                       | As at 31 December |                |                | As at<br>30 April |
|-----------------------|-------------------|----------------|----------------|-------------------|
|                       | 2012              | 2013           | 2014           | 2015              |
|                       | <i>RMB'000</i>    | <i>RMB'000</i> | <i>RMB'000</i> | <i>RMB'000</i>    |
| RMB                   | 378,937           | 292,687        | 212,159        | 128,822           |
| United States dollars | <u>50</u>         | <u>50</u>      | <u>2,862</u>   | <u>5,516</u>      |
|                       | <u>378,987</u>    | <u>292,737</u> | <u>215,021</u> | <u>134,338</u>    |

#### 19. Paid-in capital

|                                                   | Paid-in capital<br><i>RMB'000</i> |
|---------------------------------------------------|-----------------------------------|
| At 1 January 2012                                 | 131,949                           |
| Capital injection                                 | <u>26,522</u>                     |
| At 31 December 2012, 2013, 2014 and 30 April 2015 | <u>158,471</u>                    |

Pursuant to the shareholders' meeting held in February 2011, the shareholders approved the capital injection from 36 individual shareholders amounting to RMB66,441,000 which was received in 2012. Out of the total amount, RMB22,221,000 was recorded as increase of paid-in capital and the remaining balance of RMB44,220,000 was recorded as increase of capital surplus.

Pursuant to the shareholders' meeting held in October 2012, the shareholders approved the capital injection from CEC amounting to RMB20,000,000. Out of the total amount, RMB4,301,000 was recorded as increase of paid-in capital and the remaining balance of RMB15,699,000 was recorded as increase of capital surplus.

**20. Other reserves**

|                                                   | <b>Capital<br/>surplus</b><br><i>(Note (i))</i><br><i>RMB'000</i> | <b>Statutory<br/>reserve</b><br><i>(Note (ii))</i><br><i>RMB'000</i> | <b>Total</b><br><i>RMB'000</i> |
|---------------------------------------------------|-------------------------------------------------------------------|----------------------------------------------------------------------|--------------------------------|
| At 1 January 2012                                 | 50,550                                                            | 63,460                                                               | 114,010                        |
| Capital injection                                 | 59,919                                                            | –                                                                    | 59,919                         |
| Transfer to statutory reserve                     | –                                                                 | 8,260                                                                | 8,260                          |
| At 31 December 2012                               | <u>110,469</u>                                                    | <u>71,720</u>                                                        | <u>182,189</u>                 |
| At 1 January 2013                                 | 110,469                                                           | 71,720                                                               | 182,189                        |
| Transfer to statutory reserve                     | –                                                                 | 7,575                                                                | 7,575                          |
| At 31 December 2013 and 2014<br>and 30 April 2015 | <u>110,469</u>                                                    | <u>79,295</u>                                                        | <u>189,764</u>                 |

- (i) It represented the excess of capital contributed by owners of Huahong over the registered capital of Huahong.
- (ii) It represents the statutory reserve. Huahong is required to transfer 10% of the profit after tax as reported in the PRC statutory accounts to the statutory reserve until the balance reaches 50% of the registered share capital each year. This reserve can be used to reduce any losses incurred or to increase capital. Except for the reduction due to losses incurred, any other usage should not result in this reserve balance falling below 25% of the registered capital.

**21. Dividends**

For the year ended 31 December 2012, dividends of Huahong total amounting to RMB69,051,000 were declared in April 2012, which were paid in 2012.

For the year ended 31 December 2013, a dividend of Huahong amounting to RMB47,541,000 was declared in March 2013 and paid in April 2013.

For the year ended 31 December 2014, a dividend of Huahong amounting to RMB31,694,000 was declared in March 2014 and paid in April 2014. Dividends total amounting to RMB158,471,000 were declared in June 2014, which were paid in August and November 2014 amounting to RMB49,296,000 and RMB109,175,000, respectively.

For the period ended 30 April 2014, a dividend of Huahong amounting to RMB31,694,000 were declared in March 2014 and paid in April 2014.

**22. Amount due to ultimate holding company**

Amount due to ultimate holding company is unsecured, interest free, repayable on demand.

**23. Deferred government grants**

|                              | Year ended 31 December |                |               | Four months ended |               |
|------------------------------|------------------------|----------------|---------------|-------------------|---------------|
|                              | 2012                   | 2013           | 2014          | 30 April          | 2015          |
|                              | RMB'000                | RMB'000        | RMB'000       | RMB'000           | RMB'000       |
|                              |                        |                |               | (Unaudited)       |               |
| Beginning of the year/period | 82,215                 | 136,894        | 108,245       | 108,245           | 58,307        |
| Additions                    | 78,098                 | 18,523         | 13,864        | 344               | 3,467         |
| Credited to profit or loss   | (23,419)               | (47,172)       | (63,802)      | (1,169)           | (14,050)      |
| End of the year/period       | <u>136,894</u>         | <u>108,245</u> | <u>58,307</u> | <u>107,420</u>    | <u>47,724</u> |

Amount mainly represents various subsidies granted by and received from local government authorities for financing various research and development projects conducted by Huahong. These subsidies will be recognised as income over the period necessary to match with the cost that they are intended to compensate.

**24. Trade and other payables**

|                                     | As at 31 December |                |                | As at<br>30 April |
|-------------------------------------|-------------------|----------------|----------------|-------------------|
|                                     | 2012              | 2013           | 2014           | 2015              |
|                                     | <i>RMB'000</i>    | <i>RMB'000</i> | <i>RMB'000</i> | <i>RMB'000</i>    |
| Trade payables                      | 151,753           | 78,985         | 152,375        | 144,508           |
| Notes payables                      | 27,075            | 65,394         | 36,216         | 46,505            |
| Other payables to related parties   | 1,000             | –              | –              | –                 |
| Salary and welfare payables         | 30,279            | 29,301         | 23,043         | 11,497            |
| Other taxes payables                | 914               | 1,055          | 808            | 120               |
| Other payables and accrued expenses | 7,114             | 5,409          | 6,325          | 8,369             |
|                                     | <u>218,135</u>    | <u>180,144</u> | <u>218,767</u> | <u>210,999</u>    |

The ageing analysis of trade payables and notes payables was as follows:

|                                   | As at 31 December |                |                | As at<br>30 April |
|-----------------------------------|-------------------|----------------|----------------|-------------------|
|                                   | 2012              | 2013           | 2014           | 2015              |
|                                   | <i>RMB'000</i>    | <i>RMB'000</i> | <i>RMB'000</i> | <i>RMB'000</i>    |
| Current to 3 months               | 159,906           | 126,745        | 177,202        | 157,105           |
| Over 3 months and within 6 months | 8,575             | 7,428          | 2,154          | 27,398            |
| Over 6 months and within 1 year   | 1,653             | 1,457          | 5,409          | 2,231             |
| Over 1 year                       | 8,694             | 8,749          | 3,826          | 4,279             |
|                                   | <u>178,828</u>    | <u>144,379</u> | <u>188,591</u> | <u>191,013</u>    |

As at 31 December 2012, 2013 and 2014 and 30 April 2015, include in the balance of trade payables are trade payables to related parties amounted to RMB9,354,000, RMB3,025,000, RMB353,000 and RMB300,000, respectively.

The fair values of Huahong's trade and other payables approximate their carrying amounts and are denominated in RMB.

## 25. Cash generated from operations

|                                                                                         | Year ended 31 December |         |         | Four months ended<br>30 April |         |
|-----------------------------------------------------------------------------------------|------------------------|---------|---------|-------------------------------|---------|
|                                                                                         | 2012                   | 2013    | 2014    | 2014                          | 2015    |
|                                                                                         | RMB'000                | RMB'000 | RMB'000 | RMB'000                       | RMB'000 |
|                                                                                         |                        |         |         | (Unaudited)                   |         |
| Profit/(loss) before taxation                                                           | 40,430                 | 64,238  | 51,800  | (7,021)                       | (2,261) |
| Adjustment for:                                                                         |                        |         |         |                               |         |
| Depreciation of property,<br>plant and equipment                                        | 3,653                  | 5,175   | 6,513   | 2,205                         | 2,202   |
| Loss on disposal of<br>property, plant and<br>equipment                                 | 17                     | 250     | 13      | 1                             | –       |
| Interest income on short-<br>term and long-term<br>deposits                             | (1,746)                | (4,853) | (3,263) | (1,158)                       | (98)    |
| Interest income on<br>entrusted loan                                                    | –                      | –       | (2,658) | –                             | –       |
| Interest income on<br>deferred consideration                                            | (1,354)                | –       | –       | –                             | –       |
| Interest income on<br>available-for-sale<br>financial assets                            | –                      | (225)   | (3,094) | (1,554)                       | (803)   |
| Impairment provision/<br>(reversal of impairment)<br>for trade and<br>other receivables | 1,079                  | (97)    | 2,238   | 338                           | (1,869) |
| Share of result of<br>a joint venture                                                   | –                      | –       | (553)   | –                             | 473     |
|                                                                                         | 42,079                 | 64,488  | 50,996  | (7,189)                       | (2,356) |

|                                                            | Year ended 31 December |          |          | Four months ended<br>30 April |           |
|------------------------------------------------------------|------------------------|----------|----------|-------------------------------|-----------|
|                                                            | 2012                   | 2013     | 2014     | 2014                          | 2015      |
|                                                            | RMB'000                | RMB'000  | RMB'000  | RMB'000                       | RMB'000   |
|                                                            |                        |          |          | (Unaudited)                   |           |
| Change in working capital                                  |                        |          |          |                               |           |
| Inventories                                                | 25,057                 | 15,421   | (26,061) | (6,622)                       | (59,127)  |
| Trade and other receivables                                | 32,809                 | 33,964   | (4,658)  | (15,600)                      | (50,066)  |
| Trade and other payables<br>and advances from<br>customers | (55,139)               | (37,789) | 41,011   | (14,958)                      | (8,949)   |
| Deferred government grants                                 | 54,695                 | (28,649) | (49,938) | (825)                         | (10,583)  |
| Cash generated from/<br>(used in) operations               | 99,501                 | 47,435   | 11,350   | (45,194)                      | (131,081) |

## 26. Commitments

### *Operating lease commitments – where Huahong is the lessee*

As at 31 December 2012, 2013 and 2014 and 30 April 2015, Huahong has future aggregate minimum lease payable under non-cancellable operating leases for office premises are as follows:

|                                | As at 31 December |         |         | As at<br>30 April |
|--------------------------------|-------------------|---------|---------|-------------------|
|                                | 2012              | 2013    | 2014    | 2015              |
|                                | RMB'000           | RMB'000 | RMB'000 | RMB'000           |
| Not later than one year        | 4,471             | 3,631   | 2,674   | 1,578             |
| In the second to fifth<br>year | 4,929             | 1,582   | 1,653   | 1,296             |
|                                | 9,400             | 5,213   | 4,327   | 2,874             |

**27. Related party transactions and balances**

Apart from those transactions and balances disclosed in other notes, Huahong has the following significant transactions in the ordinary course of business with its related parties during the Relevant Periods:

**(a) Name and relationship with related parties**

| <b>Name of the related parties</b>                                                         | <b>Relationship with Huahong</b> |
|--------------------------------------------------------------------------------------------|----------------------------------|
| CEC                                                                                        | Ultimate holding company         |
| Huada Semiconductor<br>(華大半導體)                                                             | Direct holding company           |
| Beijing Huahong IC Design Co., Ltd.<br>(北京華虹集成電路設計<br>有限責任公司)                              | Under common control of<br>CEC   |
| Shanghai Belling Co., Ltd.<br>(上海貝嶺股份有限公司)                                                 | Under common control of<br>CEC   |
| CEC Great Wall (Changsha) information<br>technology Co., Ltd.<br>(中電長城(長沙)信息技術有限公司)        | Under common control of<br>CEC   |
| Beijing Huada Zhibao Electronic System<br>Co., Ltd. (北京華大智寶電子<br>系統有限公司)                   | Under common control of<br>CEC   |
| Beijing CEC Huada Electronic Design Co.,<br>Ltd. (北京中電華大電子設計<br>有限責任公司)                    | Under common control of<br>CEC   |
| China Electronics Smart Card Co., Ltd.<br>(中電智能卡有限責任公司)                                    | Under common control of<br>CEC   |
| Shanghai Belling Microelectronics<br>Manufacturing Co., Ltd.<br>(上海貝嶺微電子製造有限公司)            | Under common control of<br>CEC   |
| China Electronics International Exhibition<br>Advertising Co., Ltd. (中國電子國際展<br>覽廣告有限責任公司) | Under common control of<br>CEC   |
| CEC Finance                                                                                | Under common control of<br>CEC   |

| Name of the related parties                                   | Relationship with Huahong                                |
|---------------------------------------------------------------|----------------------------------------------------------|
| CEC New Vision Technology Co., Ltd. (中電新視界技術有限公司)             | Under common control of CEC                              |
| Shanghai Hongzheng Assets Management Co., Ltd. (上海虹正資產經營有限公司) | Under common control of CEC                              |
| ShenZhen Aihua Electronics Co., Ltd. (深圳市愛華電子有限公司)            | Under common control of CEC                              |
| DongGuan CEC Aihua Electronics Co., Ltd. (東莞市中電愛華電子有限公司)      | Under common control of CEC                              |
| Huahong Group                                                 | Non-controlling shareholder of Huahong, associate of CEC |
| Chongqing Huahong                                             | Joint venture of Huahong                                 |

**(b) Sales of products**

|                                                            | Year ended 31 December |               |               | Four months ended |              |
|------------------------------------------------------------|------------------------|---------------|---------------|-------------------|--------------|
|                                                            | 2012                   | 2013          | 2014          | 30 April          | 2015         |
|                                                            | RMB'000                | RMB'000       | RMB'000       | RMB'000           | RMB'000      |
|                                                            |                        |               |               | (Unaudited)       |              |
| <b>Sales of products</b>                                   |                        |               |               |                   |              |
| Beijing Huahong IC Design Co., Ltd.                        | 48,573                 | 31,966        | 27,868        | 4,900             | 6,621        |
| Shanghai Belling Co., Ltd.                                 | 3,117                  | 1,751         | 3,180         | 1,380             | 425          |
| CEC Great Wall (Changsha) information technology Co., Ltd. | 1                      | –             | 1             | 1                 | –            |
| Beijing Huada Zhibao Electronic System Co., Ltd.           | 39                     | 366           | –             | –                 | 32           |
| Beijing CEC Huada Electronic Design Co., Ltd.              | –                      | –             | 119           | –                 | –            |
| Chongqing Huahong Electronics Co., Ltd.                    | –                      | –             | 4,284         | –                 | –            |
|                                                            | <u>51,730</u>          | <u>34,083</u> | <u>35,452</u> | <u>6,281</u>      | <u>7,078</u> |

*(c) Purchase of goods and services*

|                                                                  | Year ended 31 December |               |               | Four months ended |              |
|------------------------------------------------------------------|------------------------|---------------|---------------|-------------------|--------------|
|                                                                  | 2012                   | 2013          | 2014          | 2014              | 2015         |
|                                                                  | RMB'000                | RMB'000       | RMB'000       | RMB'000           | RMB'000      |
|                                                                  |                        |               |               | (Unaudited)       |              |
| <b>Purchase of products</b>                                      |                        |               |               |                   |              |
| China Electronics Smart Card Co., Ltd.                           | 40,028                 | 28,753        | 85,761        | 30,596            | 4,163        |
| Shanghai Belling Co., Ltd.                                       | 899                    | 730           | 727           | 234               | 132          |
| Shanghai Belling Microelectronics Manufacturing Co., Ltd.        | 1,012                  | 245           | –             | –                 | –            |
| Beijing Huahong IC Design Co., Ltd.                              | –                      | –             | –             | –                 | 4,274        |
| China Electronics International Exhibition Advertising Co., Ltd. | –                      | –             | 13            | –                 | –            |
|                                                                  | <u>41,939</u>          | <u>29,728</u> | <u>86,501</u> | <u>30,830</u>     | <u>8,569</u> |

**(d) Other transactions**

|                                                | Year ended 31 December |               |                | Four months ended |            |
|------------------------------------------------|------------------------|---------------|----------------|-------------------|------------|
|                                                | 2012                   | 2013          | 2014           | 2014              | 2015       |
|                                                | RMB'000                | RMB'000       | RMB'000        | RMB'000           | RMB'000    |
|                                                | (Unaudited)            |               |                |                   |            |
| <b>Interests income on deposits</b>            |                        |               |                |                   |            |
| CEC Finance                                    | 2,451                  | 5,282         | 2,038          | 937               | 434        |
|                                                | <u>2,451</u>           | <u>5,282</u>  | <u>2,038</u>   | <u>937</u>        | <u>434</u> |
| <b>Provision of entrusted loan</b>             |                        |               |                |                   |            |
| ShenZhen Aihua Electronics Co., Ltd.           | –                      | –             | 50,000         | –                 | –          |
| DongGuan CEC Aihua Electronics Co., Ltd.       | –                      | –             | 50,000         | –                 | –          |
|                                                | <u>–</u>               | <u>–</u>      | <u>100,000</u> | <u>–</u>          | <u>–</u>   |
|                                                | <u>–</u>               | <u>–</u>      | <u>100,000</u> | <u>–</u>          | <u>–</u>   |
| <b>Interest income on entrusted loan</b>       |                        |               |                |                   |            |
| ShenZhen Aihua Electronics Co., Ltd.           | –                      | –             | 1,329          | –                 | –          |
| DongGuan CEC Aihua Electronics Co., Ltd.       | –                      | –             | 1,329          | –                 | –          |
|                                                | <u>–</u>               | <u>–</u>      | <u>2,658</u>   | <u>–</u>          | <u>–</u>   |
|                                                | <u>–</u>               | <u>–</u>      | <u>2,658</u>   | <u>–</u>          | <u>–</u>   |
| <b>Purchase of building</b>                    |                        |               |                |                   |            |
| CEC New Vision Technology Co., Ltd.            | –                      | 28,955        | –              | –                 | –          |
|                                                | <u>–</u>               | <u>28,955</u> | <u>–</u>       | <u>–</u>          | <u>–</u>   |
| <b>Properties leasing fees</b>                 |                        |               |                |                   |            |
| Shanghai Hongzheng Assets Management Co., Ltd. | 652                    | 707           | 730            | 236               | 253        |
|                                                | <u>652</u>             | <u>707</u>    | <u>730</u>     | <u>236</u>        | <u>253</u> |

*(e) Balances with related parties*

|                                                           | As at 31 December |         |         | As at    |
|-----------------------------------------------------------|-------------------|---------|---------|----------|
|                                                           | 2012              | 2013    | 2014    | 30 April |
|                                                           | RMB'000           | RMB'000 | RMB'000 | 2015     |
|                                                           |                   |         |         | RMB'000  |
| <b>Deposits</b>                                           |                   |         |         |          |
| CEC Finance                                               | 315,374           | 184,499 | 112,828 | 43,056   |
| <b>Trade receivables due from related parties</b>         |                   |         |         |          |
| Beijing Huahong IC Design Co., Ltd.                       | 41,655            | 18,550  | 25,375  | 28,606   |
| Shanghai Belling Co., Ltd.                                | 127               | 50      | 545     | –        |
| Beijing Huada Zhibao Electronic System Co., Ltd.          | –                 | 56      | –       | –        |
| Chongqing Huahong Electronics Co., Ltd.                   | –                 | –       | 3,112   | 3,112    |
| <b>Advanced proceeds to related parties</b>               |                   |         |         |          |
| China Electronics Smart Card Co., Ltd.                    | –                 | –       | 11,117  | 1,428    |
| <b>Other receivables due from related parties</b>         |                   |         |         |          |
| Huada Semiconductor                                       | –                 | –       | 3,074   | 7        |
|                                                           | 41,782            | 18,656  | 43,223  | 33,153   |
| <b>Trade payables due to related parties</b>              |                   |         |         |          |
| China Electronics Smart Card Co., Ltd.                    | 6,832             | 1,183   | –       | –        |
| Shanghai Belling Co., Ltd.                                | 1,839             | 1,600   | 111     | 58       |
| Shanghai Belling Microelectronics Manufacturing Co., Ltd. | 658               | 217     | 217     | 217      |
| Beijing Huahong IC Design Co., Ltd.                       | 25                | 25      | 25      | 25       |
| <b>Other payables due to related parties</b>              |                   |         |         |          |
| CEC                                                       | –                 | 15,000  | 15,000  | 15,000   |
| Shanghai Belling Co., Ltd.                                | 1,000             | –       | –       | –        |
|                                                           | 10,354            | 18,025  | 15,353  | 15,300   |

For each of the years ended 31 December 2012, 2013 and 2014 and the four months ended 30 April 2015, the weighted average interest rates of the deposits held at CEC Finance are 1.72%, 3.02%, 2.58% and 3.31% per annum, respectively.

The above trade and other receivables and payables are unsecured, interest-free and settled according to the contract terms.

*(f) For key management personnel compensation, please refer to note 8*

*(g) Transactions with government related entities*

Huahong is a state-owned enterprise ultimately controlled by the PRC government. The transactions between Huahong and other PRC government controlled entities are related party transactions. These transactions mainly include depositing cash in certain state-owned banks.

### **III. SUBSEQUENT FINANCIAL STATEMENTS**

No audited financial statements have been prepared by Huahong in respect of any period subsequent to 30 April 2015 up to the date of this report. No dividend or distribution has been declared or made by Huahong in respect of any period subsequent to 30 April 2015.

Yours faithfully,  
**PricewaterhouseCoopers**  
*Certified Public Accountants*  
Hong Kong

## APPENDIX IV

## UNAUDITED PRO FORMA FINANCIAL INFORMATION OF THE ENLARGED GROUP

*The following is an illustrative and unaudited pro forma statement of assets and liabilities of the Enlarged Group ("Unaudited Pro Forma Financial Information of the Enlarged Group"), which has been prepared on the basis set out below and in accordance with Rule 4.29 of the Listing Rules for the purpose of illustrating the effects of the proposed Shanghai Huahong Acquisition, as if the Shanghai Huahong Acquisition had taken place on 30 June 2015.*

The Unaudited Pro Forma Financial Information of the Enlarged Group has been prepared using accounting policies consistent with that of the Group, as set out in the published interim report of the Company for the six months ended 30 June 2015.

The Unaudited Pro Forma Financial Information of the Enlarged Group should be read in conjunction with the financial information contained in this circular.

The Unaudited Pro Forma Financial Information of the Enlarged Group has been prepared by the Directors for illustrative purposes only. Because of its hypothetical nature, the Unaudited Pro Forma Financial Information of the Enlarged Group may not give a true picture of the financial position of the Enlarged Group had the proposed Shanghai Huahong Acquisition been completed at 30 June 2015 or at any future date.

### UNAUDITED PRO FORMA FINANCIAL INFORMATION OF THE ENLARGED GROUP

|                                     | Unaudited consolidated statements of assets and liabilities of the Group as at 30 June 2015 | Pro forma adjustments |               |          |          |          | Unaudited pro forma consolidated assets and liabilities of the Enlarged Group |
|-------------------------------------|---------------------------------------------------------------------------------------------|-----------------------|---------------|----------|----------|----------|-------------------------------------------------------------------------------|
|                                     | HK\$'000                                                                                    | RMB'000               | HK\$'000      | HK\$'000 | HK\$'000 | HK\$'000 | HK\$'000                                                                      |
|                                     | Note 1                                                                                      | Note 2                | Note 6        | Note 3   | Note 4   |          |                                                                               |
| <b>ASSETS</b>                       |                                                                                             |                       |               |          |          |          |                                                                               |
| <b>Non-current assets</b>           |                                                                                             |                       |               |          |          |          |                                                                               |
| Property, plant and equipment       | 437,812                                                                                     | 43,746                | 55,472        | –        | –        |          | 493,284                                                                       |
| Investment properties               | 411,675                                                                                     | –                     | –             | –        | –        |          | 411,675                                                                       |
| Land use rights held for self-use   | 14,984                                                                                      | –                     | –             | –        | –        |          | 14,984                                                                        |
| Intangible assets                   | 8,835                                                                                       | –                     | –             | –        | –        |          | 8,835                                                                         |
| Investments in an associate         | 68,273                                                                                      | –                     | –             | –        | –        |          | 68,273                                                                        |
| Investment in a joint venture       | 21,012                                                                                      | 5,180                 | 6,569         | –        | –        |          | 27,581                                                                        |
| Other receivables                   | 507,222                                                                                     | –                     | –             | –        | –        |          | 507,222                                                                       |
| Deferred tax assets                 | 54,310                                                                                      | –                     | –             | –        | –        |          | 54,310                                                                        |
| Available-for-sale financial assets | 2,536                                                                                       | –                     | –             | –        | –        |          | 2,536                                                                         |
|                                     | <b>1,526,659</b>                                                                            | <b>48,926</b>         | <b>62,041</b> | <b>–</b> | <b>–</b> |          | <b>1,588,700</b>                                                              |

# APPENDIX IV

# UNAUDITED PRO FORMA FINANCIAL INFORMATION OF THE ENLARGED GROUP

|                                     | Unaudited<br>consolidated<br>statements<br>of assets and<br>liabilities of<br>the Group<br>as at 30 June<br>2015<br><i>HK\$'000</i><br><i>Note 1</i> | Pro forma adjustments                                                                                  |                                  |                                                                    |                                  | Unaudited<br>pro forma<br>consolidated<br>assets and<br>liabilities of<br>the Enlarged<br>Group<br><i>HK\$'000</i> |
|-------------------------------------|------------------------------------------------------------------------------------------------------------------------------------------------------|--------------------------------------------------------------------------------------------------------|----------------------------------|--------------------------------------------------------------------|----------------------------------|--------------------------------------------------------------------------------------------------------------------|
|                                     |                                                                                                                                                      | Audited assets and<br>liabilities of Huahong<br>as at 30 April 2015<br><i>RMB'000</i><br><i>Note 2</i> | <i>HK\$'000</i><br><i>Note 6</i> | Other pro forma<br>adjustments<br><i>HK\$'000</i><br><i>Note 3</i> | <i>HK\$'000</i><br><i>Note 4</i> |                                                                                                                    |
| <b>Current assets</b>               |                                                                                                                                                      |                                                                                                        |                                  |                                                                    |                                  |                                                                                                                    |
| Inventories                         | 638,113                                                                                                                                              | 157,033                                                                                                | 199,126                          | –                                                                  | –                                | 837,239                                                                                                            |
| Trade and other receivables         | 892,001                                                                                                                                              | 288,292                                                                                                | 365,570                          | –                                                                  | –                                | 1,257,571                                                                                                          |
| Taxation recoverable                | 12,299                                                                                                                                               | –                                                                                                      | –                                | –                                                                  | –                                | 12,299                                                                                                             |
| Available-for-sale financial assets | 200,987                                                                                                                                              | –                                                                                                      | –                                | –                                                                  | –                                | 200,987                                                                                                            |
| Short-term deposits and investments | 2,933,924                                                                                                                                            | 1,000                                                                                                  | 1,268                            | (909,600)                                                          | –                                | 2,025,592                                                                                                          |
| Cash and cash equivalents           | 617,393                                                                                                                                              | 134,338                                                                                                | 170,348                          | –                                                                  | (3,380)                          | 784,361                                                                                                            |
|                                     | <b>5,294,717</b>                                                                                                                                     | <b>580,663</b>                                                                                         | <b>736,312</b>                   | <b>(909,600)</b>                                                   | <b>(3,380)</b>                   | <b>5,118,049</b>                                                                                                   |
| <b>Total assets</b>                 | <b>6,821,376</b>                                                                                                                                     | <b>629,589</b>                                                                                         | <b>798,353</b>                   | <b>(909,600)</b>                                                   | <b>(3,380)</b>                   | <b>6,706,749</b>                                                                                                   |
| <b>LIABILITIES</b>                  |                                                                                                                                                      |                                                                                                        |                                  |                                                                    |                                  |                                                                                                                    |
| <b>Non-current liabilities</b>      |                                                                                                                                                      |                                                                                                        |                                  |                                                                    |                                  |                                                                                                                    |
| Unsecured corporate bonds           | 3,449,493                                                                                                                                            | –                                                                                                      | –                                | –                                                                  | –                                | 3,449,493                                                                                                          |
| Deferred tax liabilities            | 16,673                                                                                                                                               | –                                                                                                      | –                                | –                                                                  | –                                | 16,673                                                                                                             |
|                                     | <b>3,466,166</b>                                                                                                                                     | <b>–</b>                                                                                               | <b>–</b>                         | <b>–</b>                                                           | <b>–</b>                         | <b>3,466,166</b>                                                                                                   |
| <b>Current liabilities</b>          |                                                                                                                                                      |                                                                                                        |                                  |                                                                    |                                  |                                                                                                                    |
| Deferred government grants          | 100,154                                                                                                                                              | 47,724                                                                                                 | 60,517                           | –                                                                  | –                                | 160,671                                                                                                            |
| Advances from customers             | 26,041                                                                                                                                               | 1,563                                                                                                  | 1,982                            | –                                                                  | –                                | 28,023                                                                                                             |
| Trade and other payables            | 688,121                                                                                                                                              | 225,999                                                                                                | 286,579                          | –                                                                  | (1,720)                          | 972,980                                                                                                            |
| Bank and other borrowings           | 1,255,548                                                                                                                                            | –                                                                                                      | –                                | –                                                                  | –                                | 1,255,548                                                                                                          |
| Income tax payable                  | 87,554                                                                                                                                               | 12,558                                                                                                 | 15,924                           | –                                                                  | –                                | 103,478                                                                                                            |
|                                     | <b>2,157,418</b>                                                                                                                                     | <b>287,844</b>                                                                                         | <b>365,002</b>                   | <b>–</b>                                                           | <b>(1,720)</b>                   | <b>2,520,700</b>                                                                                                   |
| <b>Total liabilities</b>            | <b>5,623,584</b>                                                                                                                                     | <b>287,844</b>                                                                                         | <b>365,002</b>                   | <b>–</b>                                                           | <b>(1,720)</b>                   | <b>5,986,866</b>                                                                                                   |
| <b>Net assets</b>                   | <b>1,197,792</b>                                                                                                                                     | <b>341,745</b>                                                                                         | <b>433,351</b>                   | <b>(909,600)</b>                                                   | <b>(1,660)</b>                   | <b>719,883</b>                                                                                                     |

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## APPENDIX IV

## UNAUDITED PRO FORMA FINANCIAL INFORMATION OF THE ENLARGED GROUP

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*Notes:*

1. The balances are extracted from the unaudited consolidated balance sheet of the Group as at 30 June 2015 as set out in the published interim report of the Company for the six months ended 30 June 2015.
2. The balances are extracted from the audited balance sheet of Huahong as at 30 April 2015 included in the accountant's report of Huahong as set out in Appendix III to this circular.
3. Pursuant to the Shanghai Huahong Acquisition Agreements, the Company through its wholly-owned subsidiary has agreed to acquire a 95.64% equity interest in Huahong at a total consideration of RMB717.3 million (equivalent to approximately HK\$909.6 million). Upon Completion, Huahong will become a subsidiary of the Company.

Since Huahong and the Group are under the common control of CEC, Huahong will be accounted for in the consolidated financial statements of the Enlarged Group using the principles of merger accounting as prescribed in Accounting Guideline 5 issued by the Hong Kong Institute of Certified Public Accountants upon Completion.

The net assets of Huahong are combined using the existing book values from the controlling parties, namely CEC, perspective. No amount is recognised in consideration for goodwill or excess of acquirer's interest in the net fair value of acquiree's identifiable assets, liabilities and contingent liabilities over cost at the time of common control combination, to the extent of the continuation of the controlling party's interest.

The adjustment represents payment of the cash consideration of RMB717.3 million (equivalent to approximately HK\$909.6 million) by the Group. For the purpose of the Unaudited Pro Forma Financial Information of the Enlarged Group, 100% of the cash consideration is assumed to be paid by the Group's short-term deposits with original maturities of 3 to 6 months.

4. The estimated transaction cost for the Shanghai Huahong Acquisition was approximately HK\$4.8 million, which are mainly professional fees. Of the total transaction cost of HK\$4.8 million, HK\$1.4 million was paid before 30 June 2015 and HK\$1.7 million was accrued and captured under trade and other payables as at 30 June 2015.
5. No adjustments have been made to the Unaudited Pro Forma Financial Information of the Enlarged Group to reflect any trading results or other transactions of the Group and Huahong entered into subsequent to 30 April 2015.
6. For the purpose of the Unaudited Pro Forma Financial Information of the Enlarged Group, amounts denominated in Renminbi are converted into Hong Kong dollars at HK\$1.0 to RMB0.78861. No representation is made that the Hong Kong dollars amounts have been, could have been or may be converted to Renminbi, or vice versa, at the rate or at all.

**REPORT ON THE UNAUDITED PRO FORMA FINANCIAL INFORMATION OF THE  
ENLARGED GROUP**

*The following is the text of a report received from PricewaterhouseCoopers, Certificated Public Accountants, Hong Kong, for the purpose of incorporation in this circular.*



羅兵咸永道

**INDEPENDENT REPORTING ACCOUNTANT'S ASSURANCE REPORT ON THE  
COMPILATION OF UNAUDITED PRO FORMA FINANCIAL INFORMATION INCLUDED  
IN A CIRCULAR****TO THE DIRECTORS OF CHINA ELECTRONICS CORPORATION HOLDINGS  
COMPANY LIMITED**

We have completed our assurance engagement to report on the compilation of unaudited pro forma financial information of China Electronics Corporation Holdings Company Limited (the "Company") and its subsidiaries (collectively the "Group"), and Shanghai Huahong Integrated Circuit Co., Ltd. ("Huahong") (collectively the "Enlarged Group") by the directors of the Company (the "Directors") for illustrative purposes only. The unaudited pro forma financial information consists of the unaudited pro forma statement of assets and liabilities as at 30 June 2015 and related notes (the "Unaudited Pro Forma Financial Information"), as set out on pages IV-1 to IV-3 of the Company's circular dated 27 October 2015, in connection with the proposed acquisition of Huahong (the "Transaction") by CEC Huada Electronic Design Co., Ltd., a wholly-owned subsidiary of the Company. The applicable criteria on the basis of which the Directors have compiled the Unaudited Pro Forma Financial Information are described on pages IV-1 to IV-3 of the Company's circular dated 27 October 2015.

The Unaudited Pro Forma Financial Information has been compiled by the Directors to illustrate the impact of the Transaction on the Group's financial position as at 30 June 2015 as if the Transaction had taken place at 30 June 2015. As part of this process, information about the Group's financial position has been extracted by the Directors from the Group's financial statements for the six months ended 30 June 2015, on which a review report has been published.

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**Directors' Responsibility for the Unaudited Pro Forma Financial Information**

The Directors are responsible for compiling the Unaudited Pro Forma Financial Information in accordance with paragraph 4.29 of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the "Listing Rules") and with reference to Accounting Guideline 7 "Preparation of Pro Forma Financial Information for Inclusion in Investment Circulars" ("AG 7") issued by the Hong Kong Institute of Certified Public Accountants ("HKICPA").

**Reporting Accountant's Responsibilities**

Our responsibility is to express an opinion, as required by paragraph 4.29(7) of the Listing Rules, on the Unaudited Pro Forma Financial Information and to report our opinion to you. We do not accept any responsibility for any reports previously given by us on any financial information used in the compilation of the Unaudited Pro Forma Financial Information beyond that owed to those to whom those reports were addressed by us at the dates of their issue.

We conducted our engagement in accordance with Hong Kong Standard on Assurance Engagements 3420 "Assurance Engagements to Report on the Compilation of Pro Forma Financial Information Included in a Prospectus", issued by the HKICPA. This standard requires that the reporting accountant complies with ethical requirements and plans and performs procedures to obtain reasonable assurance about whether the Directors have compiled the Unaudited Pro Forma Financial Information in accordance with paragraph 4.29 of the Listing Rules and with reference to AG 7 issued by the HKICPA.

For purposes of this engagement, we are not responsible for updating or reissuing any reports or opinions on any historical financial information used in compiling the Unaudited Pro Forma Financial Information, nor have we, in the course of this engagement, performed an audit or review of the financial information used in compiling the Unaudited Pro Forma Financial Information.

The purpose of unaudited pro forma financial information included in a circular is solely to illustrate the impact of a significant event or transaction on unadjusted financial information of the entity as if the event had occurred or the transaction had been undertaken at an earlier date selected for purposes of the illustration. Accordingly, we do not provide any assurance that the actual outcome of the Transaction at 30 June 2015 would have been as presented.

A reasonable assurance engagement to report on whether the unaudited pro forma financial information has been properly compiled on the basis of the applicable criteria involves performing procedures to assess whether the applicable criteria used by the Directors in the compilation of the unaudited pro forma financial information provide a reasonable basis for presenting the significant effects directly attributable to the event or transaction, and to obtain sufficient appropriate evidence about whether:

- The related pro forma adjustments give appropriate effect to those criteria; and
- The unaudited pro forma financial information reflects the proper application of those adjustments to the unadjusted financial information.

The procedures selected depend on the reporting accountant's judgment, having regard to the reporting accountant's understanding of the nature of the company, the event or transaction in respect of which the unaudited pro forma financial information has been compiled, and other relevant engagement circumstances.

The engagement also involves evaluating the overall presentation of the unaudited pro forma financial information.

We believe that the evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

### **Opinion**

In our opinion:

- (a) the Unaudited Pro Forma Financial Information has been properly compiled by the Directors of the Company on the basis stated;
- (b) such basis is consistent with the accounting policies of the Group; and
- (c) the adjustments are appropriate for the purposes of the Unaudited Pro Forma Financial Information as disclosed pursuant to paragraph 4.29(1) of the Listing Rules.

**PricewaterhouseCoopers**

*Certified Public Accountants*

Hong Kong, 27 October 2015

**RESPONSIBILITY STATEMENT**

This circular, for which the Directors collectively and individually accept full responsibility, includes particulars given in compliance with the Listing Rules for the purpose of giving information with regard to the Company and Huahong. The Directors, having made all reasonable enquiries, confirm that to the best of their knowledge and belief the information contained in this circular is accurate and complete in all material respects and not misleading or deceptive, and there are no other matters the omission of which would make any statement herein or this circular misleading.

**DISCLOSURE OF INTERESTS**

As at the Latest Practicable Date, Mr. Dong Haoran, a non-executive Director, has interests in 4,672,420 shares of the Company. Save as disclosed herein, none of the Directors nor the chief executive of the Company had or was deemed to have any interests or short positions in the shares, underlying shares or debentures of the Company or any of its associated corporations (within the meaning of Part XV of the SFO) which were required to be notified to the Company and the Stock Exchange pursuant to Divisions 7 and 8 of Part XV of the SFO (including interests and short positions which they were deemed or taken to have under such provisions of the SFO), or which were required, pursuant to Section 352 of the SFO, to be entered in the register referred to therein, or which were required, pursuant to the Model Code for Securities Transactions by Directors of Listed Issuers contained in the Listing Rules, to be notified to the Company and the Stock Exchange.

Mr. Rui Xiaowu, the Chairman of the Company and a non-executive Director, is the chairman of CEC and a director of China Electronics Corporation (BVI) Holdings Company Limited (“CEC (BVI)”). Mr. Liu Hongzhou, the Vice Chairman of the Company and an executive Director, is a director of CEC (BVI). Mr. Xie Qinghua, the Managing Director of the Company and an executive Director, is also a director of CEC (BVI). Mr. Dong Haoran, a non-executive Director, is a director and the general manager of Huada Semiconductor, and a director of China Huada. Details of the shareholding of CEC, CEC (BVI), Huada Semiconductor and China Huada in the Company are set out in the paragraph headed “Substantial Shareholders” in this appendix. Save as disclosed herein, none of the Directors is a director or employee of a company which has, or is deemed to have, an interest or a short position in the shares or underlying shares of the Company which would fall to be disclosed to the Company and the Stock Exchange under the provisions of Divisions 2 and 3 of Part XV of the SFO.

None of the Directors was materially interested in any contract or arrangement subsisting as at the Latest Practicable Date which is significant in relation to the business of the Group taken as a whole.

Since 31 December 2014 (being the date to which the latest published audited consolidated financial statements of the Group were made up) up to the Latest Practicable Date, none of the Directors had any direct or indirect interest in any assets which had been acquired or disposed of by or leased to any member of the Group, or were proposed to be acquired or disposed of by or leased to any member of the Group.

**SUBSTANTIAL SHAREHOLDERS**

So far as is known to the Directors and the chief executive of the Company, as at the Latest Practicable Date, the following persons had, or were deemed to have, interests or short positions in the shares or the underlying shares of the Company which would fall to be disclosed to the Company and the Stock Exchange under the provisions of Divisions 2 and 3 of Part XV of the SFO:

| Name of Shareholder                   | Number or<br>attributable<br>number of<br>shares interested | Approximate<br>percentage or<br>attributable<br>percentage of<br>total issued share<br>capital of<br>the Company |
|---------------------------------------|-------------------------------------------------------------|------------------------------------------------------------------------------------------------------------------|
| CEC (BVI)                             | 812,500,000                                                 | 40.03%                                                                                                           |
| China Huada                           | 393,680,000                                                 | 19.39%                                                                                                           |
| Huada Semiconductor ( <i>Note 1</i> ) | 812,500,000                                                 | 40.03%                                                                                                           |
| CEC ( <i>Notes 1 and 2</i> )          | 1,206,180,000                                               | 59.42%                                                                                                           |

All the interests disclosed above represent long position in the shares of the Company.

*Notes:*

- (1) Huada Semiconductor holds 100% equity interest in CEC (BVI). Huada Semiconductor is deemed to be interested in the 812,500,000 shares of the Company held by CEC (BVI).
- (2) CEC holds 100% equity interest in each of China Huada and Huada Semiconductor and is deemed to be interested in the shares of the Company held by China Huada and Huada Semiconductor.

Save as disclosed above, there is no person known to the Directors or the chief executive of the Company who, as at the Latest Practicable Date, had, or was deemed to have, an interest or short position in the shares or the underlying shares of the Company, which would fall to be disclosed to the Company and the Stock Exchange under the provisions of Divisions 2 and 3 of Part XV of the SFO, or who was, directly or indirectly, interested in 10% or more of the nominal value of any class of share capital carrying rights to vote in all circumstances at general meetings of any member of the Group, or any option in respect of such capital.

#### **DIRECTORS' SERVICE CONTRACTS**

As at the Latest Practicable Date, none of the Directors had entered into, or proposed to enter into, any service contract with any member of the Group (excluding contracts expiring or determinable by the employer within one year without payment of compensation (other than statutory compensation)).

#### **EXPERTS AND CONSENTS**

The following are the qualifications of the experts whose name/advice and/or reports are contained in this circular:

| <b>Name</b>            | <b>Qualification</b>                                                                                                                                                            |
|------------------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Altus Capital          | A licensed corporation to conduct type 4 (advising on securities), type 6 (advising on corporate finance) and type 9 (asset management) regulated activities under the SFO      |
| PricewaterhouseCoopers | Certified Public Accountants                                                                                                                                                    |
| Shenwan                | A licensed corporation to conduct type 1 (dealing in securities), type 4 (advising on securities) and type 6 (advising on corporate finance) regulated activities under the SFO |

Each of Altus Capital, PricewaterhouseCoopers and Shenwan (collectively the “Experts”) has given and has not withdrawn its written consent to the issue of this circular with the inclusion of, where applicable, its letter(s) of advice and/or report(s) and references to its name in the form and context in which they respectively appear.

Each of the Experts was not beneficially interested in the share capital of any member of the Group and did not have any right (whether legally enforceable or not) to subscribe for or to nominate persons to subscribe for securities in any member of the Group as at the Latest Practicable Date.

Since 31 December 2014 (being the date to which the latest published audited consolidated financial statements of the Group were made up) and up to the Latest Practicable Date, each of the Experts did not have any direct or indirect interest in any assets which had been acquired or disposed of by or leased to any member of the Group, or were proposed to be acquired or disposed of by or leased to any member of the Group.

### **COMPETING INTEREST**

Mr. Rui Xiaowu, the Chairman of the Company and a non-executive Director, is the chairman of CEC. Mr. Dong Haoran, a non-executive Director, is a director and the general manager of Huada Semiconductor, a director of China Huada and a director of Huahong.

Currently, CEC, Huada Semiconductor and China Huada have subsidiaries or associates engaging in integrated circuits related businesses which compete or are likely to compete, either directly or indirectly, with the business of the Group. CEC has subsidiaries or associates engaging in the development and management of electronic information technology industrial parks related businesses which compete or are likely to compete, either directly or indirectly, with the business of the Group.

The abovementioned competing businesses are operated and managed by independent management and administration. The Board exercises independent judgment and is always acting in the interests of the Company and the Shareholders as a whole. Accordingly, the Group is capable of carrying on its business independently of, and at arm's length from, the competing businesses mentioned above.

Apart from the above, none of the Directors nor his associates is or was interested in any business, apart from the Group's business, that competes or competed or is or was likely to compete, either directly or indirectly, with the Group's business.

### **MATERIAL ADVERSE CHANGE**

As at the Latest Practicable Date, the Directors were not aware of any material adverse change in the financial or trading position of the Group since 31 December 2014, being the date to which the latest published audited consolidated financial statements of the Group were made up.

**MATERIAL CONTRACTS**

The following contracts (not being contracts entered into in the ordinary course of business) have been entered into by members of the Group within the two years immediately preceding the date of this circular, and are or may be material:

- (a) the transfer agreement dated 1 November 2013 entered into between Huada Electronics and CEC Information Technology Research Institute Co., Ltd in relation to the acquisition of a property transfer right by Huada Electronics for RMB296,374,000 and the difference between the RMB296,374,000 and the construction cost of the property, the details of which can be referred to in the announcement of the Company dated 1 November 2013;
- (b) the subscription agreement dated 9 January 2014 entered into between the Company and BNP Paribas, Hong Kong Branch and BOCI Asia Limited in relation to the issue of RMB2,750,000,000, 4.70% bonds due 2017, the details of which can be referred to in the announcement of the Company dated 10 January 2014;
- (c) the entrustment agreement dated 24 July 2014 entered into between CEC Technology and CEC Finance in relation to the provision of an entrusted loan of RMB400 million by CEC Technology to Hainan Resort Software Community Investment and Development Co., Ltd, the details of which can be referred to in the announcement of the Company dated 24 July 2014;
- (d) the placing agreement dated 17 September 2014 entered into between the Company and Shenyin Wanguo Securities (H.K.) Limited for the placing of up to 338,312,000 shares of the Company at a placing price of HK\$1.63 per share, the details of which can be referred to in the announcement of the Company dated 17 September 2014;
- (e) the construction agreement dated 30 December 2014 and entered into between Huada Electronics and CS&S Information System Engineering Co., Ltd whereby Huada Electronics has appointed CS&S Information System Engineering Co., Ltd to undertake weak current engineering work of a property located in the PRC for RMB17,540,000, the details of which can be referred to in the announcement of the Company dated 30 December 2014; and
- (f) the Shanghai Huahong Acquisition Agreements.

**LITIGATION**

As at the Latest Practicable Date, no member of the Group was engaged in any litigation, arbitration or claim of material importance and no litigation, arbitration or claim of material importance is known to the Directors to be pending or threatened against any member of the Group.

**MISCELLANEOUS**

- (a) The company secretary of the Company is Mr. Ng Kui Kwan. Mr. Ng is a member of the Institute of Chartered Accountants in England and Wales and a member of the Hong Kong Institute of Certified Public Accountants.
- (b) The registered office of the Company is at Clarendon House, 2 Church Street, Hamilton HM 11, Bermuda. The principal place of business of the Company in Hong Kong is at Room 3403, 34th Floor, China Resources Building, 26 Harbour Road, Wanchai, Hong Kong.
- (c) Tricor Abacus Limited, the Company's branch share registrar and transfer office in Hong Kong, is at Level 22, Hopewell Centre, 183 Queen's Road East, Wanchai, Hong Kong.
- (d) The English text of this circular and form of proxy shall prevail over the Chinese text.

**DOCUMENTS AVAILABLE FOR INSPECTION**

Copies of the following documents will be available for inspection at the principal place of business of the Company at Room 3403, 34th Floor, China Resources Building, 26 Harbour Road, Wanchai, Hong Kong during normal business hours on any business day from the date of this circular up to the holding of the SGM:

- (a) the bye-laws of the Company;
- (b) the material contracts referred to under the section headed "Material contracts" in this appendix;
- (c) the letter from the Independent Board Committee, the text of which is set out on pages 41 to 42 of this circular;
- (d) the letter from Altus Capital, the text of which is set out on pages 43 to 92 of this circular;
- (e) the accountant's report of Huahong from PricewaterhouseCoopers, the text of which are set out in Appendix III to this circular;

- (f) the report from PricewaterhouseCoopers on the unaudited pro forma financial information of the Enlarged Group, the text of which is set out in Appendix IV to this circular;
- (g) the written consents referred to under the section headed “Experts and consents” in this appendix;
- (h) the annual reports of the Company for the financial years ended 31 December 2013 and 2014; and
- (i) this circular.

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## NOTICE OF SGM

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### CHINA ELECTRONICS CORPORATION HOLDINGS COMPANY LIMITED

### 中國電子集團控股有限公司\*

*(Incorporated in the Cayman Islands and continued in Bermuda with limited liability)*

**(Stock Code: 00085)**

### NOTICE OF SPECIAL GENERAL MEETING

**NOTICE IS HEREBY GIVEN** that a special general meeting (the “Meeting”) of China Electronics Corporation Holdings Company Limited (the “Company”) will be held at Plaza 1-2, Lower Lobby, Novotel Century Hong Kong, 238 Jaffe Road, Wanchai, Hong Kong on 19 November 2015 at 10:00 a.m. for the purpose of considering and, if thought fit, passing, with or without amendments, the following resolutions as ordinary resolutions:

1. **“THAT** the equity transfer agreement dated 26 June 2015 and entered into between CEC Huada Electronic Design Co., Ltd (北京中電華大電子設計有限責任公司) (“Huada Electronics”), as purchaser and Huada Semiconductor Co., Ltd (華大半導體有限公司) as vendor (the “Huada Semiconductor Agreement”, details of which are set out in the circular of the Company dated 27 October 2015), in respect of the sale and purchase of the 73.43% equity interest in Shanghai Huahong Integrated Circuit Co., Ltd (上海華虹集成電路有限責任公司) (“Huahong”), at a consideration of RMB550.7 million, be and is hereby approved, and any one director of the Company and/or Huada Electronics be and is hereby authorised to do all such acts and things and execute all such documents for and on behalf of the Company and/or Huada Electronics which he considers necessary or expedient to give effect to the Huada Semiconductor Agreement and the transactions contemplated thereunder.”
2. **“THAT** the equity transfer agreement dated 26 June 2015 and entered into between Huada Electronics, as purchaser and the individual vendor(s), who are the director and/or employees of Huahong, as vendor (the “Individual Vendor Agreement(s)”, details of which are set out in the circular of the Company dated 27 October 2015), in respect of the sale and purchase of an aggregate of 9.95% equity interest in Huahong, at a consideration of RMB74.6 million, be and is hereby approved, and any one director of the Company and/or Huada Electronics be and is hereby authorised to do all such acts and things and execute all such documents for and on behalf of the Company and/or Huada Electronics which he considers necessary or expedient to give effect to the Individual Vendor Agreement(s) and the transactions contemplated thereunder.”

\* For identification purpose only

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## NOTICE OF SGM

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3. **“THAT** the equity transfer agreement dated 27 August 2015 and entered into between Huada Electronics, as purchaser and Shanghai Huahong (Group) Co., Ltd (上海華虹(集團)有限公司), as vendor (the “Supplemental Huahong Group Agreement”, details of which are set out in the circular of the Company dated 27 October 2015), in respect of the sale and purchase of the 7.62% equity interest in Huahong, at a consideration of RMB57.1 million, be and is hereby approved, and any one director of the Company and/or Huada Electronics be and is hereby authorised to do all such acts and things and execute all such documents for and on behalf of the Company and/or Huada Electronics which he considers necessary or expedient to give effect to the Supplemental Huahong Group Agreement and the transactions contemplated thereunder.”
4. **“THAT** the equity transfer agreement dated 27 August 2015 and entered into between Huada Electronics, as purchaser and the individual vendor(s), who are the director and/or employees of Huahong, as vendor (the “Remaining Shareholders Agreement(s)”, details of which are set out in the circular of the Company dated 27 October 2015), in respect of the sale and purchase of an aggregate of 4.64% equity interest in Huahong, at a consideration of RMB34.9 million, be and is hereby approved, and any one director of the Company and/or Huada Electronics be and is hereby authorised to do all such acts and things and execute all such documents for and on behalf of the Company and/or Huada Electronics which he considers necessary or expedient to give effect to the Remaining Shareholders Agreement(s) and the transactions contemplated thereunder.”
5. **“THAT** the continuing connected transactions contemplated under the 2015-2018 business services agreement dated 26 June 2015 and entered into between China Electronics Corporation Limited (中國電子信息產業集團有限公司) and the Company (the “2015-2018 Business Services Agreement”), and the proposed caps of the transactions thereunder be and are hereby approved, and any one director of the Company be and is hereby authorised to do all such acts and things and execute all such documents for and on behalf of the Company which he considers necessary or expedient to give effect to the 2015-2018 Business Services Agreement and the continuing connected transactions contemplated thereunder.”

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## NOTICE OF SGM

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6. “**THAT** the continuing connected transactions contemplated under the comprehensive financial services agreement dated 26 June 2015 and entered into between the Company and China Electronics Financial Co., Ltd (中國電子財務有限責任公司) (the “2015-2018 Financial Services Agreement”), and the proposed caps of the transactions thereunder be and are hereby approved, and any one director of the Company be and is hereby authorised to do all such acts and things and execute all such documents for and on behalf of the Company which he considers necessary or expedient to give effect to the 2015-2018 Financial Services Agreement and the continuing connected transactions contemplated thereunder.”

By Order of the Board  
**China Electronics Corporation Holdings Company Limited**  
**Ng Kui Kwan**  
*Company Secretary*

Hong Kong, 27 October 2015

*Registered office:*

Clarendon House  
2 Church Street  
Hamilton HM 11  
Bermuda

*Principal place of business*

*in Hong Kong:*  
Room 3403, 34th Floor  
China Resources Building  
26 Harbour Road  
Wanchai  
Hong Kong

*Notes:*

1. The register of members of the Company will be closed from 17 November 2015 to 19 November 2015, both days inclusive, during which period no transfer of shares of the Company will be registered. In order to be entitled to attend and vote at the Meeting, all share certificates with completed transfer forms must be lodged with the Company's branch share registrar and transfer office in Hong Kong, Tricor Abacus Limited at Level 22, Hopewell Centre, 183 Queen's Road East, Wanchai, Hong Kong not later than 4:30 p.m. on 16 November 2015.
2. Any shareholder of the Company entitled to attend and vote at the Meeting convened by the above notice is entitled to appoint another person as his proxy to attend and vote instead of him. A shareholder who is the holder of two or more shares may appoint more than one proxy to represent him and vote on his behalf at the Meeting. A proxy need not be a shareholder of the Company but must be present in person at the Meeting to represent the shareholder. If more than one proxy is so appointed, the appointment shall specify the number and class of shares in respect of which each such proxy is so appointed.

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## NOTICE OF SGM

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3. In order to be valid, the form of proxy must be duly completed and signed in accordance with the instructions printed thereon and returned together with the power of attorney or other authority (if any) under which it is signed, or a certified copy of such power or authority, to the Company's branch share registrar and transfer office in Hong Kong, Tricor Abacus Limited at Level 22, Hopewell Centre, 183 Queen's Road East, Wanchai, Hong Kong not later than 48 hours before the time appointed for holding the Meeting or any adjournment thereof. Completion and return of a form of proxy will not preclude a shareholder from attending and voting in person at the Meeting or any adjournment thereof, should he so wish.
4. In the case of joint registered holders of any shares, any one of such joint holders may vote at the Meeting, either personally or by proxy, in respect of such shares as if he was solely entitled thereto, but if more than one of such joint holders are present at the Meeting personally or by proxy, that one of the said persons so present whose name stands first in the register of members of the Company in respect of the joint holding shall alone be entitled to vote in respect thereof.