Innovax Capital

26 May 2022

To the Independent Board Committee and the Independent Shareholders

Dear Sirs,

MAJOR TRANSACTIONS; CONTINUING CONNECTED TRANSACTIONS; AND CONNECTED TRANSACTION IN RELATION TO PROVISION OF FINANCIAL ASSISTANCE

INTRODUCTION

We refer to our engagement as the independent financial adviser to the Independent Board Committee and the Independent Shareholders in relation to the transactions contemplated under the Revolving Loan Agreement, the Second Supplemental Debt Repayment Agreement and the Third Supplemental Debt Repayment Agreement, details of which are set out in the letter from the Board (the "**Board Letter**") contained in this circular (the "**Circular**") dated 26 May 2022 issued by the Company, of which this letter forms part. Capitalised terms used in this letter shall have the same meanings as defined in the Circular unless the context otherwise requires.

Reference is made to the announcements of the Company dated 31 March 2022 and 16 May 2022 in relation to (i) the Revolving Loan Agreement; (ii) the Second Supplemental Debt Repayment Agreement; and (iii) the Third Supplemental Debt Repayment Agreement. Details of the Agreements are set forth in the below section headed "Principal Factors and Reasons Considered — Terms and reasons for and benefits of the Agreements — 1. Principal Terms" below.

As at Latest Practicable Date, Zhejiang Yongli owns 65% equity interest in Guizhou Yongli and Guizhou Yongli is interested in approximately 55.29% of the issued share capital of the Company and hence the controlling shareholder of the Company (as defined under the GEM Listing Rules). Accordingly, each of Zhejiang Yongli and Guizhou Yongli is a connected person of the Company. Zhejiang Yongli is principally engaged in investment holding in the PRC and Guizhou Yongli is principally engaged in investment holding in the PRC. Zhejiang Yongli is owned by Mr. Zhou Yongli and his spouse, Ms. Xia Wanmei of approximately 94.25% and 3.49% respectively.

As (i) the highest applicable percentage ratio calculated in respect of the provision of financial assistance and annual cap in the amount of RMB35,000,000 under the Revolving Loan Agreement exceeds 25%, the Revolving Loan Agreement and the transactions contemplated thereunder

constitute a major transaction and continuing connected transaction on the part of the Company and are subject to the reporting, announcement and Independent Shareholders' approval requirements under the GEM Listing Rules; and (ii) the highest applicable percentage ratio calculated in respect of the provision of financial assistance under the Second Supplemental Debt Repayment Agreement and the Third Supplemental Debt Repayment Agreement exceed 25%, the Second Supplemental Debt Repayment Agreement and the Third Supplemental Debt Repayment Agreement and the transactions contemplated thereunder constitute a major transaction and connected transaction on the part of the Company and are subject to the reporting, announcement and Independent Shareholders' approval requirements under the GEM Listing Rules.

The EGM will be convened and held, *inter alia*, for the respective Independent Shareholders to consider and, if thought fit, ratify the Revolving Loan Agreement and the transactions contemplated thereunder and approve the Second Supplemental Debt Repayment Agreement, the Third Supplemental Debt Repayment Agreement and the transactions contemplated thereunder. Ms. He Lianfeng ("**Ms. He**"), an executive Director and her spouse totally have approximately 0.039% of interest in Zhejiang Yongli, the ultimate holding company of the Company. Mr. Xia Zhenbo ("**Mr. Xia**"), a non-executive Director is beneficially interested in 640,000 H Shares of the Company. Accordingly, Ms. He and Mr. Xia are considered to have a material interest under the Agreements and have abstained from voting at the Board meeting for approving the transactions contemplated under the Agreements. Save as disclosed herein, no other Director has a material interest in the Agreements and is therefore not required to abstain from voting at the Board meeting.

The Independent Board Committee, comprising all the independent non-executive Directors (namely Mr. Yu Weidong, Mr. Zhang Jiangyong and Mr. Yuan Lingfeng), has been formed to advise the Independent Shareholders in respect of the Agreements and the transactions contemplated thereunder.

We, Innovax Capital Limited, have been appointed as the Independent Financial Adviser to advise the Independent Board Committee and the Independent Shareholders on the fairness and reasonableness in respect of the Agreements and the transactions contemplated thereunder. As at the Latest Practicable Date, we are not connected with the Directors, chief executive and substantial Shareholders of the Company, or Zhejiang Yongli and its designated parties, or Guizhou Yongli, or any of their respective subsidiaries or associates and are therefore considered suitable to give independent advice to the Independent Board Committee and the Independent Shareholders. We have not provided any other services to the Company in the last two years prior to the date of the Circular. Apart from normal professional fees payable to us by the Company in connection with this appointment, no arrangement exists whereby we have received or will receive any fees or benefits from the Company or the Directors, chief executive and substantial Shareholders of the Company or Zhejiang Yongli and its designated parties or Guizhou Yongli or any of their respective subsidiaries or associates or any other parties that could reasonably be regarded as relevant to our independence. Accordingly, we consider that we are independent pursuant to Rule 17.96 of the GEM Listing Rules.

BASIS OF OUR OPINION

In formulating our opinion, we have relied on the accuracy of the information and representations contained in the Circular and have assumed that all information and representations made or referred to in the Circular were true, accurate and complete in all material respects at the time they were made and continue to be true, accurate and complete in all material respects at the date of this Circular and continue to be so up to the date of the EGM, and Independent Shareholders will be informed of any material change of information in the Circular as soon as possible up to the date of the EGM. We have also relied on our discussion with the management of the Company (the "**Management**") and its representatives regarding the Group and the representatives on the Agreements and the transactions contemplated thereunder, including the information and representations contained in the Circular. We have also assumed that all statements of belief, opinion and intention made by the Management and its representatives respectively in the Circular were reasonably made after due enquiry.

We consider that we have reviewed sufficient information to reach an informed view, to justify our reliance on the accuracy of the information contained in the Circular and to provide a reasonable basis for our advice. We have no reason to suspect that any material facts have been omitted or withheld from the information contained or opinions expressed in the Circular nor to doubt the truth, accuracy and completeness of the information and representations provided to us by the Management and its representatives. We have not, however, conducted an independent in-depth investigation into the business and affairs of the Group, or their respective associates, nor have we carried out any independent verification of the information supplied.

PRINCIPAL FACTORS AND REASONS CONSIDERED

In arriving at our opinion in respect of the fairness and reasonableness in respect of the Agreements and the transactions contemplated thereunder, we have taken into consideration the following principal factors and reasons:

A. Background information of the Group

The Group is a PRC-based company principally engaged in (i) the manufacture and sales of woven fabrics; (ii) the provision of woven fabrics subcontracting services; and (iii) assets management services; and (iv) investment advisory services. The Group operates its business in the PRC, Europe, South America, Middle East and other overseas regions.

Set forth below are the summary of the financial performance of the Group for the year ended 31 December 2019, 2020 and 2021 and the financial position of the Group as at 31 December 2019, 2020 and 2021, as extracted from the Company's annual report for the year ended 31 December 2020 (the "**FY2020 Annual Report**") and for the year ended 31 December 2021 (the "**FY2021 Annual Report**").

	For the year ended 31 December		
	2019	**2020**	**2021**
	RMB'000	*RMB'000*	*RMB'000*
	(audited)	(audited)	(audited)
Revenue	134,537	77,980	98,184
— *Woven fabrics*	130,315	74,929	93,263
— *Subcontracting services*	4,222	2,751	4,921
— *Investment advisory services*	—	300	—
Finance costs	(5,929)	(6,587)	(2,017)
Loss for the year	(49,166)	(28,691)	(18,820)

	As at 31 December		
	2019	**2020**	**2021**
	RMB'000	*RMB'000*	*RMB'000*
	(audited)	(audited)	(audited)
Bank balances and cash	46,896	31,635	30,968
Net current assets	83,554	70,382	63,178
Total assets	331,951	293,307	276,887
Amount due to immediate holding company	38,472	16,236	18,253
Total liabilities	84,649	55,051	55,716
Net assets	247,302	238,256	221,171
Net cash used in operating activities	(4,877)	(3,232)	(2,773)

As extracted from FY2020 Annual Report, the Group's revenue decreased from approximately RMB134.5 million for the year ended 31 December 2019 to approximately RMB78.0 million for the year ended 31 December 2020, representing a decrease of approximately 42.0%. Such decrease was mainly attributable to both of domestic and export sales of woven fabrics and subcontracting income as a result of the long-lasting outbreak of the novel coronavirus epidemic leading to the decline in demand of the product of the Group from both local and overseas customers.

The Group's loss for the year decreased from approximately RMB49.2 million for the year ended 31 December 2019 to approximately RMB28.7 million for the year ended 31 December 2020, representing a decrease of approximately 41.6%. Such decrease was mainly due to (i) the absence of impairment loss of interests in associates for the year ended 31 December 2020; (ii) decrease in administrative expenses mainly due to decrease in salary, staff

welfare expenses, travelling expenses and various office administrative expense resulted from suspension of work and business activities due to the control over the COVID-19 epidemic since early 2020; and partially offset by (iii) decrease in revenue as discussed above.

As extracted from FY2021 Annual Report, the Group's revenue increased from approximately RMB78.0 million for the year ended 31 December 2020 to approximately RMB98.2 million for the year ended 31 December 2021, representing an increase of approximately 25.9%. Such increase was mainly due to the increase in revenue from both manufacture and sales of woven fabrics and subcontracting fee income. Despite the increase in revenue, the Group's gross profit decreased from approximately RMB2.4 million for the year ended 31 December 2020 to approximately RMB450,000 for the year ended 31 December 2021, mainly due to the decrease in selling price in both domestic and export sales of woven fabric, increase in wages and rise of cost of raw materials as a result of shortage of labour force and substantial appreciation of renminbi, and rise of freight cost caused by delay of transportation as a result of the COVID-19 epidemic.

The Group's loss of the year decreased from approximately RMB28.7 million for the year ended 31 December 2020 to approximately RMB18.8 million for the year ended 31 December 2021, representing a decrease of approximately 34.4%. Such decrease was mainly due to (i) decrease in finance costs on imputed interest on non-current interest-free amount due to immediate holding company; (ii) decrease in loss on disposal of a subsidiary and (iii) decrease in share of result of an associate.

B. Terms and reasons for and benefits of the Agreements

1. *Principal terms of the Agreements*

(i) *the Revolving Loan Agreement*

Below are the principal terms of the Revolving Loan Agreement:

Date:	31 March 2022 (after trading hours of the Stock Exchange)
Parties:	(i) The Company (as the lender); and (ii) Zhejiang Yongli (as the borrower)
Revolving Loan:	an unsecured revolving loan granted by the Company or its subsidiary to Zhejiang Yongli or its designated parties from time to time during the Availability Period in the principal amount of up to RMB35,000,000
Availability Period:	1 January 2021 to 31 March 2022

Interest: the Company is entitled to Loan Interest at the relevant loan prime rate issued by the National Interbank Funding Centre accruing from the date of grant of the relevant Revolving Loan up to the repayment date. From 1 January 2021 to 7 December 2021, the corresponding interest rate charged on the Revolving Loan was 3.85%. From 20 December 2021 to 19 January 2022, the Corresponding Interest Rate was 3.80%. From 20 January 2022 to 31 March 2022, the Corresponding Interest Rate was 3.70%.

(ii) *the Second Supplemental Debt Repayment Agreement*

Below are the principal terms of the Second Supplemental Debt Repayment Agreement:

Date: 31 March 2022 (after trading hours of the Stock Exchange)

Parties:
(i) The Company;
(ii) Guizhou Yongli; and
(iii) Zhejiang Yongli

Details:
(i) as at the date of the Second Supplemental Debt Repayment Agreement, the Company is indebted to Guizhou Yongli the Shareholder's Loan in the total outstanding amount of RMB218,474,890.06 and the Company agreed to repay in advance part of the Shareholder's Loan in the amount of RMB30,000,000 to Guizhou Yongli;

(ii) upon receipt of the payment of RMB30,000,000 from the Company, Guizhou Yongli agreed (a) to waive part of the Shareholder's Loan in the amount of RMB30,000,000; (b) the Shareholder's Loan be set off against the equivalent amount of the Loan Interest on dollar-for-dollar basis and upon which the Loan Interest would be repaid in full; and

(iii) upon completion of the above repayment in advance, waiver of part of the Shareholder's Loan and the set off of Shareholder's Loan against the Loan Interest, the Company will be indebted to Guizhou Yongli the Shareholder's Loan in the total outstanding amount of RMB157,330,134.06, which will be settled by the Company in accordance with the Settlement Arrangement agreed by the parties under the Supplemental Debt Repayment Agreement.

(iii) *the Third Supplemental Debt Repayment Agreement*

Below are the principal terms of the Third Supplemental Debt Repayment Agreement:

Date:	16 May 2022 (after trading hours of the Stock Exchange)
Parties:	(i) The Company; (ii) Guizhou Yongli; and (iii) Zhejiang Yongli
Details:	(i) as at the date of the Third Supplemental Debt Repayment Agreement, the Company is indebted to Guizhou Yongli the Shareholder's Loan in the total outstanding amount of RMB218,474,890.06 and the Company agreed to repay in advance part of the Shareholder's Loan in the amount of RMB18,000,000 (instead of RMB30,000,000 previously agreed under the Second Supplemental Debt Repayment Agreement) to Guizhou Yongli, which will be settled by the internal resources of the Company;

(ii) upon receipt of the payment of RMB18,000,000 from the Company, Guizhou Yongli agreed (a) to waive part of the Shareholder's Loan in the amount of RMB18,000,000; (b) the Shareholder's Loan be set off against the equivalent amount of the Loan Interest on dollar-for-dollar basis and upon which the Loan Interest would be repaid in full;

(iii) upon completion of the above repayment in advance, waiver of part of the Shareholder's Loan and the set off of Shareholder's Loan against the Loan Interest, the Company will be indebted to Guizhou Yongli the Shareholder's Loan in the total outstanding amount of RMB181,330,134.06, which will be settled by the Company in accordance with the Settlement Arrangement agreed by the parties under the Supplemental Debt Repayment Agreement.

As the repayment in advance of part of the Shareholder's Loan in the amount of RMB18,000,000 will be settled by the internal resources of the Company, the Second Supplemental Debt Repayment Agreement and the Third Supplemental Debt Repayment Agreement are conditional upon and subject to the satisfaction of the condition of the approval of the Independent Shareholders at the EGM to be convened to approve the Second Supplemental Debt Repayment Agreement and the Third Supplemental Debt Repayment Agreement and the transactions contemplated thereunder in accordance with the requirements under the GEM Listing Rules having been obtained only and are no longer subject to the obtaining of any bank loan by the Company.

The above condition is not waivable and if the above condition has not been satisfied on or before 15 July 2022 (or such later date as may be agreed between the parties), the Company shall repay the total outstanding amount of the Shareholder's Loan according to the Settlement Arrangement and Zhejiang Yongli shall, within 10 days upon receipt of the written notice from the Company that the above conditions cannot be satisfied, repay the Loan Interest in the total amount of RMB1,144,756 to the Company.

As at the Latest Practicable Date, the above condition remained unfulfilled.

2. *Background and reasons for and benefits of the Agreements*

(i) *the Revolving Loan Agreement*

As stated in the Board Letter, the Revolving Loan was first granted by the Company on 4 January 2021, since then, the Revolving Loan were granted by the Company or its subsidiary to Zhejiang Yongli or its designated parties at the request of Zhejiang Yongli from time to time due to its short-term working capital needs especially under the current COVID-19 pandemic situation. During the Availability Period, the Reveling Loan were granted by the Company or its subsidiary to Zhejiang Yongli or its designated parties at the request of Zhejiang Yongli from time to time and there had been repayments made by Zhejiang Yongli and its designated parties from time to time depending on their working capital position. As such, on the condition that the business operation of the Company was not affected and the Company has sufficient idle cash, the Company or its subsidiary agreed to grant the Revolving Loan to Zhejiang Yongli or its designated parties during the Availably Period and the Company would be able to receive interest income in return. As further advised by the Management, all outstanding principal amount of the Revolving Loan had been repaid to the Company as at the date of the Revolving Loan Agreement. We understand from the Management that the Revolving Loan Agreement was entered into by Company and Zhejiang Yongli to record, confirm and agree on as well as to govern the arrangements concerning the Revolving Loan and to re-comply with the requirement to enter into a written agreement for connected transactions under Rule 20.32 of GEM Listing Rules in relation to the grant of the Revolving Loan. The Company will also earn interest under the terms of the Revolving Loan Agreement.

In assessing the fairness and reasonableness of the Revolving Loan Agreement, we have considered:

(a) the financial position and cash availability of the Group

Based on the financial statements of the Group as at 31 December 2020 and 31 December 2021, the Group has bank balances and cash of approximately RMB31.6 million and RMB31.0 million respectively. In addition, based on the bank and cash balances record of the Group, the Group has at all time maintained positive bank balances and cash during the Availability Period. As confirmed by the Management, such balance of cash was more than sufficient for the working capital needs of the Group's operation. In addition, based on the monthly bank balances record of the Group, the Group maintained sufficient bank balance for its daily operation. As further confirmed by the Management, the Group did not encounter any liquidity problem during the Availability Period.

(b) Default risk

As stated in the Letter from the Board, the use of the Revolving Loan by Zhejiang Yongli was due to its short-term working capital needs especially under the current COVID-19 pandemic situation. According to a schedule of the Revolving Loan and repayment record provided by the Company, we noted that there had been repayment of the Revolving Loan from Zhejiang Yongli from time to time and among the loans granted during the Availability Period, the period of repayment by Zhejiang Yongli was in fact no longer than 29 days. Further, we have selected and checked to four repayment records during the Availability Period, including the final repayment record confirming that all outstanding principal amount of the Revolving Loan had been repaid from Zhejiang Yongli and its designated parties to the Company. The Company represented that there has been no loan granted to Zhejiang Yongli subsequent to the Revolving Loan was fully paid. Prior to the Revolving Loan was granted, the Group also obtained the latest financial statements of Zhejiang Yongli in order to assess its financial health. In this regard, we have obtained and checked the financial statements of Zhejiang Yongli for the two years ended 31 December 2021 and noted that Zhejiang Yongli was in net assets position during the respective years.

Having considered that Zhejiang Yongli (i) repaid the Revolving Loan quickly with no longer than 29 days during the Availability Period; (ii) had no default history; (iii) had net assets during the two years ended 31 December 2021; and (iv) had no outstanding loan as at the date of the Revolving Loan Agreement, we concur with the Management that there was no default risk of loans granted to Zhejiang Yongli.

(c) Interest rates and terms of maturity of the Revolving Loan Agreement

Pursuant to the Revolving Loan Agreement, the Company is entitled to Loan Interest at the relevant loan prime rate issued by the National Interbank Funding Centre accruing from the date of grant of the relevant Revolving Loan up to the repayment date. We have obtained the calculation schedules of the loan interests in respect of the Revolving Loan during the Availability Period and reperformed the calculation thereof. According to the calculation schedules, the loan interest rates applied in the calculation were 3.80% and 3.85% during the year ended 31 December 2021, and 3.70% and 3.80% during the three months ended 31 March 2022. We noted that such interest rates were in line with the one-year loan prime rate as published monthly by the People's Bank of China during the Availability Period. Given the Availability Period was about one year, we considered the interest rate of the Revolving Loan by benchmarking with the one-year loan prime rate is reasonable. As further advised by the Management, the Group's idle cash were mainly placed in banks in the PRC or as demand deposits in banks in the PRC. As at the Latest Practicable Date, the prevailing benchmark interest rate for demand deposits in the PRC as promulgated by the People's Bank of China was approximately 1.50% per annum. Therefore, it is more favourable to the Group and the Shareholders to receive interests from the Revolving Loan with interest rate ranged from 3.70% to 3.85% per annum than placing the idle cash in banks as demand deposits.

In addition, in order to assess the fairness and reasonableness of the interest rate of the Revolving Loan, we have conducted independent research from the public domain on comparable transactions (the "**Comparable Transactions**") which (i) were announced by companies listed on the Stock Exchange from 1 January 2022 and up to 31 March 2022 (the "**Review Period**"), which in our view represents a sufficient period of time to reflect the prevailing market conditions for conducting such transactions as the Review Period covers the entire Availability Period; (ii) involved the provision of financial assistances by way of loans by companies listed in Hong Kong; (iii) constituted connected transactions of the issuers under the Listing Rules or GEM Listing Rules. Shareholders should note that the business, operations, and prospects of the Comparable Transactions may not be identical to those of the Company and we have not conducted any in-depth investigation into the respective businesses and operations of the Comparable Transactions. However, we consider that the Comparable Transactions could provide a general reference as to the common market practice of companies listed in Hong Kong for conducting similar transactions under the Revolving Loan Agreement. To the best of our knowledge and on a best-effort basis, we have identified an exhaustive list of 29 Comparable Transactions which fit our selection criteria.

Set forth below is a comparison of the Comparable Transactions during the Review Period:

	Name of Company	Stock Code	Date of announcement	Interest rate per annum	Term to maturity (month)
1	Sun Art Retail Group Limited	6808	9 March 2022	3.70%	12
2	JW (Cayman) Therapeutics Co. Ltd	2126	6 March 2022	3.60%	12
3	51 Credit Card Inc.	2051	31 January 2022	5.80%	36
4	Xinyuan Property Management Service (Cayman) Ltd.	1895	12 January 2022	Nil(Note 1)	4
5	Allied Group Limited	373	4 January 2022	10.00%	15
6	Petro-King Oilfield Services Limited	2178	30 December 2021	8.00%	12
7	Joy City Property Limited	207	16 December 2021	1.50%(Note 2)	12
8	Touyun Biotech Group Limited	1332	10 December 2021	12.00%	2
9	Bojun Education Company Limited	1758	8 December 2021	4.75%	36
10	Most Kwai Chung Limited	1716	19 November 2021	1.50%(Note 3)	60
11	TCL Electronics Holdings Limited	1070	11 November 2021	8.00%(Note 4)	36
12	51 Credit Card Inc.	2051	14 September 2021	5.80%	36
13	Cheshi Holdings Limited	1490	12 September 2021	6.00%	36
14	Legend Holdings Corporation	3396	10 August 2021	7.50%(Note 5)	36
15	Lee's Pharmaceutical Holdings Limited	950	16 July 2021	4.00%	12
16	Zhi Sheng Group Holdings Limited	8370	2 June 2021	6.00%	30
17	GBA Holdings Limited	261	1 June 2021	7.00%	24
18	Lee's Pharmaceutical Holdings Limited	950	28 May 2021	4.00%	12
19	China Glass Holdings Limited	3300	29 April 2021	7.00%	12
20	Smart-Core Holdings Limited	2166	28 April 2021	8.00%	12
21	Lee's Pharmaceutical Holdings Limited	950	28 April 2021	4.00%	12
22	Cogobuy Group	400	16 April 2021	6.00%	36
23	Lee's Pharmaceutical Holdings Limited	950	26 March 2021	4.00%	12
24	China Communications Construction Company Limited	1800	5 February 2021	7.50%	Not disclosed
25	Greentown China Holdings Limited	3900	5 February 2021	7.50%	Not disclosed
26	Lee's Pharmaceutical Holdings Limited	950	1 February 2021	4.00%	12
27	Kader Holdings Company Limited	180	22 January 2021	12.00%	36
28	Baiying Holdings Group Limited	8525	15 January 2021	5.00%	11
29	China Jinmao Holdings Group Limited	817	14 January 2021	6.53%(Note 6)	12
			Maximum	**12.00%**	**60**
			Minimum	**0.00%**	**2**
			Average	**5.89%**	**21**
	The Company			**3.70% to 3.85%**	**15**

Source: Announcements of the relevant companies involved in the Comparable Transactions on the website of the Stock Exchange

Note 1: As disclosed in the announcement of Xinyuan Property Management Service (Cayman) Ltd. ("**Xinyuan**") dated 12 January 2022, there were two loans amounting to a total of approximately HK$110.9 million provided by Xinyuan to its controlling shareholder in March 2020. The loans were provided for the purpose of offshore funding needs by the controlling shareholder. As stated in the announcement of Xinyuan, the board of Xinyuan did not submit the abovementioned transactions for the approval by its independent shareholders since the loans were fully repaid on 30 June 2020.

Note 2: As disclosed in the announcement of Joy City Property Limited dated 16 December 2021, the interest of the loan was referenced to the prevailing benchmark interest rate for demand deposits in the PRC as promulgated by the People's Bank of China from time to time. As at the Latest Practicable Date, the prevailing benchmark interest rate for demand deposits in the PRC as promulgated by the People's Bank of China is 1.5% per annum, as announced by the website of PBOC. For comparison purpose only, demand deposit rate of 1.5% per annum was taken for the analysis of the Comparable Transactions. Further, the loan was provided by a property development company held jointly by (i) an indirectly wholly-owned subsidiary of Joy City Property Limited; and (ii) the connected person as an early distribution of profit to them on a pro-rata basis according to their shareholding interest in the project company.

Note 3: As disclosed in the announcement of Most Kwai Chung Limited dated 19 November 2021, a wholly-owned subsidiary of Most Kwai Chung Limited provided a back-to-back loan to company held by its connected person for the sole purpose of such connected person providing the shareholders' loan to a joint venture company held by Most Kwai Chung Limited and such connected person.

Note 4: As disclosed in the announcement of TCL Electronics Holdings Limited dated 11 November 2021, for illustration purpose, as at 30 September 2021, the historical interest rates of unsecured loans under the master financial agreement (TCL Holdings) (2020–2022) ranged from 3.2% to 8.0%. For comparison purpose only, the highest interest rate was taken for the analysis of the Comparable Transactions.

Note 5: As disclosed in the announcement of Legend Holdings Corporation dated 10 August 2021, During the term, the interest rate of each shareholder loan to be and guarantee fees provided by the Company or its subsidiaries to Better Education and its subsidiaries shall not be lower than the prevailing costs of financing obtained by the company in the market. Depending on actual situations, the interest rates of shareholder loans shall not be lower than the prevailing interest rates of borrowings obtained from independent third-party banks or financing institutions or the interest rates of the corporate bonds issued by the company. As per the interim report of Legend Holdings Corporation for the period ended 30 June 2021, the annual interest rates of its bonds listed as of 30 June 2021 ranged from 0% to 7.50%. For comparison purpose only, the highest interest rate was taken for the analysis of the Comparable Transactions.

Note 6: As disclosed in the announcement of China Jinmao Holdings Group Limited dated 14 January 2021, the interest of the loan is by reference to the loan prime rate for the loans of the same term as published by the National Interbank Funding Center from time to time, subject to a floating range of 50% higher or lower than such rate. For comparison purpose only, the highest interest rate was taken for the analysis of the Comparable Transactions.

As shown from the above table, we observed that:

(1) the interest rates of the Comparable Transactions ranged from nil to 12.00% per annum with an average of approximately 5.89% per annum. The interest rate of the Revolving Loan of 3.70% to 3.85% is within the range of the Comparable Transactions. There are also certain Comparable Transactions involving larger loan amount but with nil or lower interest rate. For instance, the loans provided by Xinyuan Property Management Service (Cayman) Ltd (Stock Code: 1895) in aggregate amounted to approximately HK$111.9 million were at nil interest rate, and the loans provided by Joy City Property Limited (Stock Code: 207) amounted to RMB1,100 million were at interest rate of 1.5% per annum;

(2) the interest rate of the Revolving Loan was near the low-end range of Comparable Transaction and was lower than the average interest rate of the Comparable Transactions. Despite such, we noted that (i) out of the 29 Comparable Transactions, the interest rates for 14 Comparable Transactions were lower than the average interest rates of approximately 5.89% per annum; and (ii) among the 15 Comparable Transactions which interest rates were higher than the average interest rates of approximately 5.89% per annum, after excluding the Comparable Transactions for China Communication Construction Company Limited (Stock Code: 1800) and Greentown China Holdings Limited (Stock Code: 3900) where term to maturity were not disclosed, the term to maturity for seven Comparable Transactions (out of the remaining 13 Comparable Transactions) were longer than the Availability Period of the Revolving Loan and therefore, it is reasonable for them to charge a higher interest rate. Based on the aforesaid and also taken in account the fact that Zhejiang Yongli has granted the Shareholder's Loan to the Group since September 2011 which was interest-free, we are of the view that the interest rate of the Revolving Loan, although was lower than the average interest rate of the Comparable Transactions and was near the low-end range of Comparable Transaction, is reasonable and not exceptional; and

(3) the terms to maturity of the Comparable Transactions ranged from two months to 60 months with an average term to maturity of approximately 21 months. The term of the Revolving Loan of 15 months falls within the range and below the average of that of the Comparable Transactions.

(d) Annual cap of the Revolving Loan Agreement

Pursuant to the Revolving Loan Agreement, the annual caps on the maximum outstanding principal amount for the Revolving Loan and during Availability Period (i.e. 1 January 2021 to 31 March 2022) were RMB35.0 million. According to the schedule of the Revolving Loan provided by the Company, the maximum principal outstanding amount for the Revolving Loan was approximately RMB34.9 million for the year ended 31 December 2021 and RMB28.2 million for the three months ended 31 March 2022.

As disclosed in the Board Letter, the annual caps have been determined after taking into consideration of the following, among other things:

(1) the maximum outstanding principal amount of the Revolving Loan advanced by the Company or its subsidiary to Zhejiang Yongli or its designated parties during the Availability Period was in the amount of RMB34,900,0000;

(2) as at the date of the Revolving Loan Agreement, Zhejiang Yongli has repaid the Company all outstanding principal amount of the Revolving Loan; and

(3) as at the date of the Revolving Loan Agreement, Zhejiang Yongli is indebted to the Company Loan Interest in the total amount of RMB1,144,756.

In assessing the fairness and reasonableness of the proposed annual caps, we have discussed with the Management to understand the principal bases and assumptions used in the determination of the proposed annual caps. We have also reviewed the detailed schedule of Revolving Loan balance and noted that historical maximum outstanding principal amount of Revolving Loan during the Availability Period was RMB34.9 million. Since the Availability Period is over and Zhejiang Yongli has repaid the Company all outstanding principal amount of the Revolving Loan, we are of the view that the proposed annual caps are fair and reasonable so far as the Independent Shareholders are concerned and is in the interests of the Company and the Shareholders as a whole.

Based on the above, considering that (i) the Company has sufficient idle cash and the Revolving Loan was granted without affecting the normal business operation of the Company; and (ii) there is no default risk on the principal amount of the Revolving Loan as all outstanding principal amount of the Revolving Loan had been repaid to the Company and no Revolving Loan has been granted to Zhejiang Yongli and its designated parties subsequent to the Availability Period and up to the Latest Practicable Date; (iii) the Company would be able to receive interest income of approximately RMB1.1 million in return at average interest rate

of approximately 3.70% to 3.85% per annum, which is higher than the prevailing benchmark interest rate for demand deposit in the PRC as promulgated by the People's Bank of China of 1.50% per annum; and (iv) the annual caps are fair and reasonable, we concur with the view of the Management that the Revolving Loan Agreement and the transactions contemplated thereunder are, although not in the ordinary and usual course of business of the Group, are in normal commercial terms and in the interest of the Company and the Shareholders as a whole.

(ii) *the Second Supplemental Debt Repayment Agreement and the Third Supplemental Debt Repayment Agreement*

As stated in the Board Letter, since 23 December 2016, the Company has been indebted to Guizhou Yongli the Shareholder's Loan in the total outstanding amount of approximately RMB239,677,000. On 30 November 2020, the Company and Guizhou Yongli entered into the Supplemental Debt Repayment Agreement, pursuant to which it was agreed that the total outstanding amount of the Shareholder's Loan was in the amount of RMB218,475,000.06 as at the date of the Supplemental Debt Repayment Agreement and the Settlement Arrangement was agreed between the parties as follows:

(a) in the first and second year from the date of the Supplemental Debt Repayment Agreement (i.e. for the two years ended 31 December 2022), the Company would not be required to make any repayment;

(b) in the third to seventh year from the date of the Supplemental Debt Repayment Agreement (i.e. for the five years ended 31 December 2027), the Company would be required to make repayment in the amount of RMB800,000 on or before 31 March of each year; and

(c) in 2028 and onwards, the Company would be required to make repayment on an annual basis, the amount of which should not exceed 50% of the Company's operating cash flow for that year until the full repayment of the total outstanding Shareholder's Loan.

The Shareholder's Loan is unsecured and interest free.

Pursuant to the Third Supplemental Debt Repayment Agreement, the Company agreed to repay in advance part of the Shareholder's Loan in the amount of RMB18,000,000 to Guizhou Yongli and in return, (i) Guizhou Yongli agreed to waive part of the Shareholder's Loan in the amount of RMB18,000,000 and that the Shareholder's Loan be set off against the equivalent amount of the Loan Interest on dollar-for-dollar basis and upon which the Loan Interest would be repaid in full; and (ii) the total outstanding amount of the Shareholder's Loan will be reduced to RMB181,330,134.06 and will be settled by the Company in accordance with the Settlement Arrangement agreed by the parties under the Supplemental Debt

Repayment Agreement. As stated in the Board Letter, as Guizhou Yongli agreed to waive part of the Shareholder's Loan in the amount of RMB18,000,000, it is commercially justifiable for the Company to repay in advance part of the Shareholder's Loan in the amount of RMB18,000,000 and the amount of the Shareholder's Loan agreed to be waived by Guizhou Yongli will be settled by internal resources of the Company.

On 23 May 2022, the Company, Guizhou Yongli and Zhejiang Yongli entered into the Undertaking Letter pursuant to which Guizhou Yongli and Zhejiang Yongli are willing to continue to support the Company by irrevocably and unconditionally undertake to the Company that, (i) should the repayment in advance of part of the Shareholder's Loan in the amount of RMB18,000,000 to Guizhou Yongli under the Third Supplemental Debt Repayment Agreement will cause any liquidity problem of the Group in the future, they will provide the Supporting Loan in the amount of up to RMB18,000,000 to the Company upon the request of the Company from time to time from the date of the undertaking letter up to the full repayment of the Shareholder's Loan and the Supporting Loan will be interest free and the repayment terms will be the same as the Settlement Arrangement (i.e. in the first and second year from the date of grant of the Supporting Loan, the Company would not be required to make any repayment, in the third to seventh year from the date of grant of the Supporting Loan, the Company would be required to make repayment in the amount of RMB800,000 on or before 31 March of each year and in the eighth year and onwards, the Company would be required to make repayment on an annual basis, the amount of which should not exceed 50% of the Company's operating cash flow for that year until the full repayment of the total outstanding loan); and (ii) by providing the Supporting Loan to the Company pursuant to the Undertaking Letter, the waiver of part of the Shareholder's Loan in the amount of RMB18,000,000 by Guizhou Yongli under the Third Supplemental Debt Repayment Agreement will remain valid and will not be revoked.

We concur with the Management's view that it is commercially justifiable for the Company to early repay the amount of RMB18,000,000 in return of the waiver of RMB18,000,000 of the Shareholder's Loan. The early repay discount represents approximately 8.2% of the Shareholder's Loan with a total amount of RMB218,475,000.06. Also, there is no guarantee that the Guizhou Yongli will continue to agree to waive part of the Shareholder's Loan if the Group were to repay the Shareholder's Loan at a later point in time.

Taking into consideration the above and also the undertaking from Guizhou Yongli, we are of the view that the Second Supplemental Debt Repayment Agreement and the Third Supplemental Debt Repayment Agreement provide the Company an opportunity to reduce the Shareholder's Loan. Therefore, we concur with the view of the Management that the Second Supplemental Debt Repayment Agreement and the Third Supplemental Debt Repayment Agreement and the

transactions contemplated thereunder are, although not in the ordinary and usual course of business of the Group, the terms are fair and reasonable and are in the interest of the Company and the Shareholders as a whole.

3. ***Review of internal control and risk management procedures in respect of the Revolving Loan Agreement***

As disclosed in the Board Letter, during the review of the annual results of the Company for the year ended 31 December 2021, the Revolving Loan was discovered and investigated by the supervisory committee of the Company and it was noted that the Revolving Loan would have constituted a major transaction for provision of financial assistance and continuing connected transaction on the part of the Company under the GEM Listing Rules. As advised by the Management, the failure by the Company to comply with the reporting, announcement and Independent Shareholders' approval requirements under the GEM Listing Rules in respect of the Revolving Loan was due to the oversight of the Company and unintentional.

Upon becoming aware of the incidents, the management of the Group has sought professional advice from its legal advisors immediately as to the requirements under the GEM Listing Rules for Revolving Loan. The Company was informed that the Revolving Loan would constitute a financial assistance from the Group to its connected person, and that the Company would not have complied in full with the requirements under Chapter 19 and Chapter 20 of the GEM Listing Rules. In the circumstances, the Company has immediately taken all initiatives to re-comply with the GEM Listing Rules as soon as it can. The Revolving Loan Agreement was entered into by the respective parties to record, confirm and agree on as well as to govern the arrangements concerning the Revolving Loan from the Company to Zhejiang Yongli, and to re-comply with the requirement to enter into a written agreement for connected transactions under Rule 20.32 of GEM Listing Rules. The Company will also benefit from the interest income under the terms of the Revolving Loan Agreement.

In order to prevent the occurrence of similar non-compliance incident in the future and to comply with the requirements under the GEM Listing Rules, the Company has taken or will take the following remedial actions:

(i) the Company had reviewed other bank remittances made by the Company and checked whether it is necessary for the Company to comply with any requirements under the GEM Listing Rules. Save as disclosed in the Announcement, the Company did not discover other transaction which would be required to comply with the requirements under the GEM Listing Rules;

(ii) the Company has published the announcement dated 31 March 2022 in relation to the Revolving Loan Agreement and the Second Supplemental Debt Repayment Agreement to inform the shareholders of the details of, among other things, the Revolving Loan;

(iii) the Company will issue a circular containing the details of the Revolving Loan to the shareholders and will convene the EGM for the independent shareholders to approve, confirm and ratify the Revolving Loan;

(iv) the Company has issued a memorandum to the Board and senior management of the Company to report the incident of non-compliance of GEM Listing Rules in relation to the Revolving Loan and to reiterate the importance to strictly follow the Internal Control Measures adopted by the Company on 29 April 2022 to ensure that the Company will be able to comply with the applicable requirements under the GEM Listing Rules, and in case of any doubt, the Company will consult external legal advisers, financial advisers and/or the Stock Exchange in advance;

(v) the Company has engaged Avista PRO-Risk Advisory Limited (the "**Internal Control Consultant**") to conduct an internal control review particularly in relation to the bank remittance and operation of bank accounts, the procedures of connected transaction and notifiable transaction of the Company and implement the necessary measures to enhance the internal control of the Company, considering that the Internal Control Consultant (i) is independent from the Company; and (ii) has solid experience advising more than 800 companies of a wide range of trades in different aspects, including but not limited to internal control and risk management, environmental, social and governance advisory, and initial public offerings. The Internal Control Consultant is in the course of conducting the internal control review and the first review is expected to be completed on or before 31 May 2022. The Company will make further announcement(s) in relation to the result of the internal control review and measures (if any) to be implemented to enhance the internal control of the Company as and when appropriate; and

(vi) the relevant personnel(s) of the Group will attend a director training in relation to the requirements under Chapters 19 and 20 of the GEM Listing Rules to get himself familiar with the requirements under the GEM Listing Rules and to ensure that he will procure the Company to comply with the requirements under the GEM Listing Rules in the future on or before 31 May 2022 after dispatch of the circular in mid May 2022.

In this regard, we have reviewed the record and enquired with the Management in relation to the details of such internal control and risk management procedures, in particular (i) the memorandum to the Board the senior management of the Company on the non-compliance of GEM Listing Rules in relation to the Revolving Loan; (ii) internal guidelines adopted and updated by the Company in December 2019 in relation to Chapters 19 and 20 of the GEM Listing Rules; and (iii) the internal control procedures in relation to Chapters 19 and 20 of the GEM Listing Rules. In addition, the Management has also reviewed the relevant records of the Group and confirmed that no other connected transactions of the Company are not in full compliance with the GEM Listing

Rules. Based on the above, we concur with the Management's view that adequate measures were in place to ensure full compliance with the GEM Listing Rules by the Company in future and the interests of the Shareholders would be safeguarded.

C. Financial effect of the Agreements

(i) ***Earnings***

Pursuant to the Revolving Loan Agreement, the Company is entitled to receive an interest with reference to the relevant loan prime rate issued by the National Interbank Funding Centre accruing from the date of grant of the relevant Revolving Loan up to the repayment date. Subject to the passing of the resolution(s) to be proposed at the EGM to rectify the Revolving Loan Agreement, the Company will earn interests from the Revolving Loan amounting to approximately RMB1.1 million and such interest income is expected to be recorded in the income statement for the year ending 31 December 2022. Further, as a result of the partial early repayment of the Shareholder's Loan under the Second Supplemental Debt Repayment Agreement and the Third Supplemental Debt Agreement, assuming the imputed interest rate on the outstanding amount of the Shareholder's Loan remains unchanged at 12.42%, the finance cost calculated as per imputed interest rate on the outstanding amount of the Shareholder's Loan would also be reduced in each year. As a result of the above, the earnings attributable to shareholders of the Company will be enhanced for the year ending 31 December 2022.

(ii) ***Net asset value***

Saved for the expected increase in earnings resulting from the interest on the Revolving Loan during the year ending 31 December 2022, it is expected that there is no material impact on net asset value from the Revolving Loan Agreement.

On the other hand, under the Third Supplemental Debt Repayment Agreement, the Company intends to settle the partial early repayment of the Shareholder's Loan of RMB18,000,000 by internal resources of the Company. Since the outstanding amount of the Shareholder's Loan is carrying at fair value discounted at an imputed interest rate of 12.42% in the Group's financial statement, it is expected that the Group's net asset value will decrease as a result. In relation to the carrying amount of the Shareholder's Loan, it is worth noting that the calculation of which involved various prudent assumptions. Should the future financial performance of the Group improve beyond the Management's prudent expectation, the abovementioned carrying amount would be different.

(iii) ***Gearing ratio***

In view of the above financial effects, in particular, the decrease in net asset value of the Group, it is expected that the gearing ratio will increase resulted from the Second Supplemental Debt Repayment Agreement and the Third Supplemental Debt Repayment Agreement.

It is expected that there is no material impact on gearing ratio from the Revolving Loan Agreement.

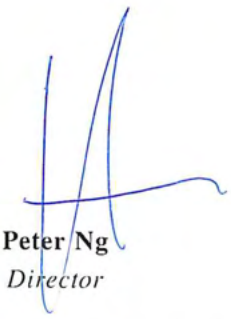
Shareholders should note that the above analysis are for illustrative purpose only and do not purport to represent the financial position of the Group as a result of the Agreements.

RECOMMENDATION

Having taken into consideration the factors and reasons as stated above, we are of the opinion that the terms of the Revolving Loan Agreement and the Third Supplemental Debt Repayment Agreement the Second Supplemental Debt Repayment Agreement are although not in ordinary course of business of the Group, are on normal commercial terms, and are fair and reasonable so far as the Independent Shareholders are concerned and are in the interests of the Company and the Shareholders as a whole. Accordingly, we recommend the Independent Board Committee to advise the Independent Shareholders to vote in favor of the resolutions to be proposed at the EGM to rectify the Revolving Loan Agreement and the transactions contemplated thereunder and approve the Second Supplemental Debt Repayment Agreement, the Third Supplemental Debt Repayment Agreement the transactions contemplated thereunder in this regard.

Yours faithfully,
For and on behalf of
Innovax Capital Limited

Richard Chu
Managing Director



Peter Ng
Director

Note: Richard Chu and Peter Ng are licensed persons under the SFO to carry out Type 1 (dealing in securities) and Type 6 (advising on corporate finance) regulated activities under the SFO and regarded as responsible officers of Innovax Capital Limited. Richard Chu and Peter Ng have over 15 years and 10 years of experience in corporate finance industry, respectively.