八方金融有限公司
OCTAL Capital Limited

29 July 2021

To the Independent Board Committee and the Independent Shareholders

Dear Sirs,

(I) SUBSCRIPTION OF SHARES UNDER SPECIFIC MANDATE; AND (II) APPLICATION FOR WHITEWASH WAIVER

INTRODUCTION

We refer to our engagement as the Independent Financial Adviser to the Independent Board Committee and the Independent Shareholders in respect of the Subscription and the transactions contemplated thereunder and the Whitewash Waiver, details of which are contained in the circular to the Shareholders dated 29 July 2021 (the "Circular"), of which this letter forms part. Unless the context requires otherwise, capitalised terms used in this letter shall have the same meanings as those defined in the Circular.

As set out in the letter from the Board (the "Letter from the Board") of the Circular, on 28 May 2021, the Company entered into the Subscription Agreement with the Subscriber, pursuant to which, the Company has conditionally agreed to allot and issue, and the Subscriber has conditionally agreed to subscribe for a maximum of 11,252,732,911 Subscription Shares at the Subscription Price of HK$0.059 per Subscription Share for a total consideration of not more than RMB554,381,000.

The 11,252,732,911 Subscription Shares represent approximately (i) 166.27% of the issued share capital of the Company as at the date of the Latest Practicable Date; and (ii) 62.44% of the enlarged fully paid up issued share capital of the Company upon Completion.

The allotment and issuance of the Subscription Shares is subject to approval by the Independent Shareholders at the EGM to be convened and held. Resolutions will be proposed at the EGM to approve, among other things, the Specific Mandate to allot and issue the Subscription Shares under the Subscription Agreement.

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As at the Latest Practicable Date, the Subscriber and parties acting in concert with it (including the Fund, the General Partner, the Limited Partners and the Investment Manager and their respective ultimate beneficial owners) do not own or have control or direction over any Shares. Upon Completion, the Subscriber will hold a maximum of 11,252,732,911 Shares, representing approximately 62.44% of the enlarged fully paid up issued share capital of the Company (assuming there is no other change in the issued share capital of the Company save for the allotment and issuance of the Subscription Shares pursuant to the Subscription).

Under Rule 26.1 of the Takeovers Code, upon the allotment and issuance of the Subscription Shares at Completion, the Subscriber would be obliged to make a mandatory general offer to the Shareholders for all the issued Shares and other securities of the Company not already owned or agreed to be acquired by the Subscriber and parties acting in concert with it unless the Whitewash Waiver is granted by the Executive and the approval by 75% of the Independent Shareholders at the EGM by way of poll is obtained in accordance with the Takeovers Code. In this regard, an application has been made to the Executive for the Whitewash Waiver in respect of the allotment and issuance of the Subscription Shares.

INDEPENDENT BOARD COMMITTEE

An Independent Board Committee, comprising all three (3) independent non-executive Directors, namely Mr. Hu Yuming, Mr. Lin Lei and Mr. Zhang Xiaoya, has been formed to advise the Independent Shareholders as to whether the terms of the Subscription Agreement and the transactions contemplated thereunder as well as the Whitewash Waiver are fair and reasonable and on how to vote at the EGM. None of the members of the Independent Board Committee has any interest or involvement in the transactions contemplated under the Subscription Agreement or the Whitewash Waiver. The two (2) non-executive Directors, namely Mr. Wang Zhenyu and Mr. Zhang Jianxing, are not taking part in the Independent Board Committee due to (i) both of them being the employees of CDH Investments Management (Hong Kong) Limited, an affiliate of the general partner of CDH Fund IV, L.P., which indirectly holds the entire equity interests in CDH; and (ii) Mr. Wang Zhenyu's indirect interests in CDH.

We, Octal Capital Limited, have been appointed by the Company with approval from the Independent Board Committee to advise the Independent Board Committee in respect of the Subscription Agreement and the transactions contemplated thereunder as well as the Whitewash Waiver.

OUR INDEPENDENCE

As at the Latest Practicable Date, we (i) were not connected with the directors, chief executives and substantial Shareholders, the Subscriber or any of their respective subsidiaries or associates or parties acting in concert with any of them; and (ii) do not have any shareholding, directly or indirectly, in any members of the Group or any right (whether legally enforceable or not) to subscribe for or to nominate persons to subscribe for securities in any member of the Group. Therefore, we are considered independent and suitable to give independent advice to the Independent Board Committee and the

Independent Shareholders. During the last two years, there was no engagement between the Company or the Subscriber and us. Apart from normal professional fee payable to us by the Company in connection with this appointment, no arrangement exists whereby we will receive any fees or benefits from the Group or the Directors, chief executive and substantial Shareholders or the Subscriber or any of its subsidiaries or their respective associates, and any parties acting in concert with them.

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 at the time they were made and continue to be true as at the Latest Practicable Date. We have also relied on our discussions with the management of the Company regarding the Group, the Subscriber and the Subscription including the information and representations contained in the Circular. We have also assumed that all statements of belief, opinion and intention made by the Directors and the Company 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 Directors. We have not, however, conducted an independent in-depth investigation into the business and affairs of the Group, the Subscriber and their respective associates nor have we carried out any independent verification of the information supplied.

As set out in the responsibility statement in Appendix II to the Circular, the Directors collectively and individually accept full responsibility for the Circular, which includes particulars given in compliance with the Listing Rules for the purpose of giving information with regard to the Company. The Directors, having made all reasonable enquiries, confirm that to the best of their knowledge and belief, the information contained in the 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 in the Circular misleading.

The Directors jointly and severally accept full responsibility for the accuracy of the information contained in the Circular and confirm, having made all reasonable inquiries, that to the best of their knowledge, opinions expressed in the Circular have been arrived at after due and careful consideration and there are no other facts not contained in the Circular, the omission of which would make any statement in the Circular misleading.

Should there be any material changes after the Latest Practicable Date, we will notify the Independent Board Committee and the Independent Shareholders as soon as possible.

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OCTAL Capital Limited

PRINCIPAL FACTORS AND REASONS CONSIDERED

In formulating our opinion and recommendation in respect of the Subscription and the Whitewash Waiver, we have taken into account the following principal factors and reasons:

1. **Background to and reasons for the Subscription**

   (i) Information of the Company and the Subscriber

   The Company

   The Company is a company incorporated in the Cayman Islands with limited liability and the issued Shares of which are listed on the Main Board of the Stock Exchange. The Group is principally engaged in the (i) manufacture and sale of automobile accessories; (ii) trading of automobile accessories; and (iii) operation of 4S dealership stores and related business.

   The Subscriber

   The Subscriber is a company incorporated in Hong Kong with limited liability and an indirect 99.11%-owned subsidiary of the Fund, which is managed by the Investment Manager. For details of the background and shareholding structure of the Subscriber, please refer to the section headed "Information of Subscriber" in the Letter from the Board.

(ii) Financial information of the Group

Review of financial performance

Set out below is a summary of the consolidated financial information of the Group for the years ended 31 December 2018 ("FY2018"), 2019 ("FY2019") and 2020 ("FY2020") as extracted from the annual reports of the Group for FY2019 (the "2019 Annual Report") and FY2020 (the "2020 Annual Report") respectively:

	FY2018 (audited) *RMB'000*	FY2019 (audited) *RMB'000*	FY2020 (audited) *RMB'000*
Segment revenue			
– The manufacturing business	595,182	468,050	536,837
– The wholesale business	234,747	61,285	20,814
– Automobile dealership and service business	582,954	1,221,297	354,076
Total revenue from continuing operations	**1,412,883**	**1,750,632**	**911,727**
Cost of sales and services	(1,252,705)	(1,610,550)	(807,316)
Segment gross profits			
– The manufacturing business	94,774	72,553	86,424
– The wholesale business	18,990	10,757	3,975
– Automobile dealership and service business	46,414	56,772	14,012
Total gross profits from continuing operations	**160,178**	**140,082**	**104,411**
Profit/(Loss) for the year from continuing operations attributable to			
– Shareholders of the Company	146,038	(159,947)	(466,748)
– Non-controlling interests	(15,670)	(13,599)	(6,910)
Total	130,368	(173,546)	(473,658)

FY2018 vs FY2019

The Group recorded total revenue from continuing operations of approximately RMB1,750.6 million for FY2019, representing an increase of approximately RMB337.7 million or 23.9% as compared to that for FY2018. The increase in revenue was primarily attributable to the consolidation of revenue from the automobile dealership and services business through completion of the acquisition of such segment in September 2018. Besides, the Group recorded gross profit from continuing operations of approximately RMB140.1 million for FY2019, representing a decrease of approximately RMB20.1 million or 12.6% as compared to the same of approximately RMB160.2 million for FY2018. The decrease in gross profit was mainly due to (i) the decrease in revenue of the wholesale service business and manufacturing business for FY2019 as compared with FY2018; and (ii) the decline in gross profit margin in the automotive dealership and services business as a result of the overall downturn in China's automotive sales industry during FY2019.

The Group recorded net loss from continuing operations attributable to the Shareholders of approximately RMB159.9 million for FY2019, as compared to the net profit of approximately RMB146.0 million due to (i) the increase in cost of sales and services of approximately RMB357.8 million; (ii) the decrease in other revenue and gains and loss of approximately RMB240.5 million as a result of the decline in fair value change in the embedded derivative financial instruments in relation to the convertible notes in the principal amount of USD35 million due in 2019 and the decrease in interest income recorded from loans made by the Group; and (iii) the increase of distribution costs of approximately RMB47.2 million.

FY2019 vs FY2020

The Group recorded total revenue from continuing operations of approximately RMB911.7 million for FY2020, representing a significant decrease of approximately RMB838.9 million or 47.9% as compared to that for FY2019. The decline in revenue was primarily attributable to the impact of the COVID-19 pandemic on the Group, which led to a significant decrease in revenue from the wholesale service business and the automobile dealership and service business of the Group. Furthermore, the Group recorded gross profit from continuing operations of approximately RMB104.4 million for FY2020, representing a decrease of approximately RMB35.7 million or 25.5% as compared to the same of approximately RMB140.1 million for FY2019. The decrease in gross profit was mainly due to the significant decrease in revenue from the wholesale service business and the automobile dealership and service business of the Group for FY2020 as compared with FY2019.

The Group recorded net loss from continuing operations attributable to the Shareholders of approximately RMB466.7 million for FY2020, representing an increase of approximately RMB306.8 million or 191.8% as compared to the same for FY2019. The loss for the year from continuing operations was magnified as a result of the decrease in revenue and the increase in allowance for expected credit losses on trade receivables, deposits, prepayments and other receivables and amounts due from related parties (the "Impairment Loss on Receivables"). The Impairment Loss on Receivables was mainly attributable to the other receivables owed by Inner Mongolia Lifeng Dingsheng Automobile Co., Ltd.* (內蒙古利豐鼎盛汽車有限公司) and its subsidiaries and associates. For details of the Impairment Loss on Receivables, please refer to the paragraph headed "Collection of Receivables" in the 2020 Annual Report.

Review of financial position

Set out below is the summary of the audited consolidated statement of financial position of the Group as at 31 December 2018, 2019 and 2020 as extracted from the 2019 Annual Report and the 2020 Annual Report:

Summary of statements of financial position

	As at 31 December		
	2018 (audited) *RMB'000*	2019 (audited) *RMB'000*	2020 (audited) *RMB'000*
Non-current assets	494,651	365,408	278,559
Current assets	2,075,506	1,571,823	1,012,673
– Cash and cash equivalent	134,460	64,697	64,564
Total assets	**2,570,157**	**1,937,231**	**1,291,232**
Non-current liabilities	22,010	116,485	163,456
Current liabilities	1,562,723	1,009,147	854,921
Total liabilities	**1,584,733**	**1,125,632**	**1,018,377**
Net assets	**985,424**	**811,599**	**272,855**
Bank and other borrowings:			
– Current portion	552,309	489,982	286,595
– Non-current portion	–	–	54,149
Total Bank and other borrowings	**552,309**	**489,982**	**340,744**
Gearing ratio *(Note)*	**160.8%**	**138.7%**	**373.2%**

Note: Gearing ratio represents total liabilities divided by net assets.

As at 31 December 2019

As at 31 December 2019, the total assets of the Group amounted to approximately RMB1,937.2 million, with current assets of approximately RMB1,571.8 million and non-current assets of approximately RMB365.4 million. The current assets mainly included inventories of approximately RMB202.8 million and deposit, prepayments and other receivables of approximately RMB1,119.2 million, which represented approximately 10.5% and 57.8% of the total assets, respectively.

As at 31 December 2019, the Group's total liabilities amounted to approximately RMB1,125.6 million, with current liabilities of approximately RMB1,009.1 million and non-current liabilities of approximately RMB116.5 million. The current liabilities were mainly comprised of (i) bank and other borrowings of approximately RMB490.0 million; (ii) trade payables of approximately RMB238.9 million; and (iii) accruals and other payables of RMB181.8 million, which represented 43.5%, 21.2% and 16.1% of the total liabilities, respectively. As disclosed in the 2019 Annual Report, the secured and interest-bearing bank and other loans have remaining terms within 1 year and effective interest rates ranging from 3.48% to 13.80%.

As at 31 December 2019, the Group recorded net assets of approximately RMB811.6 million and the gearing ratio of the Group slightly decreased from approximately 160.8% as at 31 December 2018 to approximately 138.7% as at 31 December 2019, which indicated that the Group maintained a similar level of financial leverage.

As at 31 December 2020

As at 31 December 2020, the total assets of the Group amounted to approximately RMB1,291.2 million, with current assets of approximately RMB1,012.6 million and non-current assets of approximately RMB278.6 million. The current assets mainly included (i) inventories of approximately RMB131.5 million; (ii) trade receivables of approximately RMB161.2 million; and (iii) deposit, prepayments and other receivables of approximately RMB654.8 million, which represented approximately 10.2%, 12.5% and 50.7% of the total assets, respectively.

As at 31 December 2020, the Group's total liabilities amounted to approximately RMB1,018.4 million, with current liabilities of approximately RMB854.9 million and non-current liabilities of approximately RMB163.5 million. The current liabilities were mainly comprised of (i) bank and other borrowings of approximately RMB286.6 million; (ii) trade payables of approximately RMB283.5 million; and (iii) accruals and other payables of RMB201.3 million, which represented 28.1%, 27.8% and 19.8% of the total liabilities, respectively. As disclosed in the 2020 Annual Report, all of the bank and other borrowings bear fixed interest rates ranging from 5.00% to 13.80%.

As at 31 December 2020, the Group recorded net assets of approximately RMB272.9 million and the gearing ratio of the Group significantly increased from approximately 138.7% as at 31 December 2019 to approximately 373.2% as at 31 December 2020, which indicated that the financial leverage of the Group deteriorated during FY2020. As disclosed in the 2020 Annual Report, the increase in gearing ratio was mainly due to the recognition of the Impairment Loss on Receivables.

(iii) Reasons for and benefits of the Subscription

As stated in the Letter from the Board, the Board was informed by the Investment Manager and noted that with the recovery of the automobile market and the vigorous development of new energy vehicles ("NEV"), the Fund continues to be optimistic about the development direction of the automobile industry and vigorously deploys related industries upstream and downstream. After communicating with the Qingdao Laixi Municipal Government through the Investment Manager, the Company and the Fund considered that they are highly compatible with each other, and the Qingdao Laixi Municipal Government strongly supports the auto parts industry and the investment by the Fund through the Subscription. The Directors are also of the view that the Subscription represents a good opportunity for the Company to introduce a strategic investor with strong local government support and to raise sufficient funds to enhance its capabilities in product development and upgrade its manufacturing infrastructure and sales platforms, and further expand the scale of product production and improve operating efficiency. The funds raised under the Subscription can also strengthen the Company's capital base and be utilized towards repayment of outstanding bank loans which will help significantly reduce the Company's capital cost and improve its financial position.

The maximum gross proceeds to be raised from the Subscription is HK$663,911,241.749. The maximum net proceeds to be raised from the Subscription is estimated to be approximately HK$662 million, of which

(i) approximately HK$480 million will be applied for enhancement of the Company's manufacturing capability:

  (a) as to approximately HK$70 million for purchase of land use rights in Economic Development Zone, Laixi City, Qingdao City, Shandong Province for construction of new production plants in late 2021 or first half of 2022;

  (b) as to approximately HK$360 million for construction of new production plants and other supporting facilities including warehouse, research and development center, office building, staff dormitory and showroom on the lands through the above purchase of land use rights in Shandong Province to expand the Group's production capacity and technology capability for its manufacturing business. The construction work is expected to commence from late 2021 and be completed by 2023; and

  (c) as to approximately HK$50 million for purchase of related production equipment in the PRC for production of automotive parts for NEV, mainly including inverters and multifunctional mobile power supplies, to broaden the Group's product portfolio and pursue opportunities to expand its exposure in the NEV industry;

(ii) approximately HK$120 million will be applied for repayment of the outstanding bank loans of the Group; and

(iii) approximately HK$62 million will be applied as general working capital of the Group:

(a) as to approximately HK$44 million for the procurement costs of the Group's manufacturing business and automobile dealership and service business;

(b) as to approximately HK$10 million for the remuneration of the Group's employees; and

(c) as to approximately HK$8 million for the Group's other daily expenses (including professional fees payable to the Group's legal advisers and auditors).

Optimisation of business portfolio and relief of financial pressure

As disclosed in the section headed "Financial information of the Group" in this letter, the Group has been suffering from (i) continuous loss from operations which amounted to approximately RMB173.5 million and RMB473.7 million for the FY2019 and FY2020 respectively and (ii) decreasing net assets from approximately RMB811.6 million as at 31 December 2019 to RMB272.9 million as at 31 December 2020. The worsening financial performance and position of the Group were mainly attributable to unsatisfactory operating results of the Group's automobile dealership and service business. In FY2020, the Group's automobile dealership and service business recorded a significant annual decline in revenue of approximately 71.0%, which led to a significant annual increase in segment loss of approximately 218.5% when compared to that for FY2019. In view of the deteriorating financial performance of the Group's automobile dealership and service business, the Group entered into equity transfer agreements with two independent third parties in FY2020 to dispose of its subsidiaries which were principally engaged in the relevant businesses. On the other hand, as mentioned in the section headed "Financial Information of the Group" above in this letter, the Group's manufacturing business is the only business segment of the Group which recorded revenue growth and segment profit for FY2020 as a result of the active sourcing of new customers, optimisation of customer and product structure, as well as the increase in selling price of products for certain customers. According to the 2020 Annual Report, the Group will assess its existing businesses and consider appropriate disposal of relevant businesses with long-term loss and uncertain prospects, so as to optimise resources allocation and improve the Group's profitability. Moreover, to further improve its manufacturing business and achieve turnaround results in the coming years, the Group will enhance management efficiency and capture market opportunities through an optimised organisational structure, more team incentives and further resource integration. Therefore, the Subscription is in line with the development strategies of the Group to optimise its existing business portfolio by streamlining the operation of automobile dealership and service business and reallocate its resources to focus on and expand its manufacturing business which is relatively more profitable.

As disclosed in the 2020 Annual Report, as at 31 December 2020, the Group recorded current liabilities of RMB854.9 million, which mainly consisted of (i) bank and other borrowings of approximately RMB286.6 million (which were repayable within 12 months) and (ii) trade payables of approximately RMB283.5 million. The bank and other borrowings bear fixed interest rates of up to 13.8% per annum, and the Group incurred finance costs of approximately RMB42.9 million in FY2020, accounting for approximately 41.1% of the Group's gross profit. As mentioned above, the Group only had cash and bank balance of approximately RMB64.6 million as at 31 December 2020 which are not sufficient to settle the aforesaid liabilities. Therefore, the Group is in need of funding to fulfil its debt repayment obligation and reduce the finance costs arising from the bank and other borrowings, and thus alleviate the financial pressure of the Group.

Industry prospect

During the year 2020, the global economy has taken a hit from the COVID-19 pandemic, and economic activities in the PRC, including the production and consumption of automotive products in the PRC have been affected. According to the statistics of China Association of Automobile Manufacturers, approximately 25.3 million new vehicles were sold in 2020 in the PRC, representing an annual decline of approximately 1.9% and marking its third straight annual decline since 2018. The annual decline in sales in the automobile industry in the PRC signaled a negative performance of automobile dealership industry.

As an upstream production line in the supply chain of the automotive industry, the automotive parts market was disrupted by the continuous slowdown of the global automotive industry in 2020. The shutdown of production lines and implementation of government policies restricting the movement of goods and labour as a preventive measure to the COVID-19 pandemic had severely disrupted the supply chains of the automotive industry in the first half of 2020. The impact on the supply chains of the automotive industry had in turn led to a decrease in the demand for the automotive parts manufacturing business. With reference to data released by General Administration of Customs of the People's Republic of China (中華人民共和國海關總署) ("GAC") on 18 January 2021 regarding the statistics of import and export amount, the total export amount of automotive parts for FY2020 amounted to USD56.5 billion, representing a year-on-year decline of approximately 6.6%, which demonstrated a relatively weak performance in the demand of automotive parts for year 2020, when compared to year 2019. However, the automotive parts market showed a strong sign of recovery in the first quarter of year 2021 as proven by the drastic increase in the export amount of automotive parts as compared to the same period in year 2020. According to the data released by GAC on 18 April 2021, the export amount of automotive parts hit USD17.8 billion for the first three months ended 31 March 2021, representing an increase of approximately 39.1% as compared to the same for the first quarter of 2020. In addition to the increase in spending on automobile following the trend of global economic recovery, the improvement in the growth rate of export amount is expected to persist as a result of the promotion of NEV.

As a result of a new round of global scientific and technological revolution and further industrial reform, the automobile industry is facing a period of major change and moving towards full electrification. Despite the overall decline of sales in the automobile market in 2020, the production and sales of NEV have risen in contrast to the downturn of the general automobile industry, with production and sales reaching 1.36 million units and 1.37 million units, which represented an increase of approximately 7.5% and 10.9%, respectively. Driven by the tide of NEV development across the board, it is expected that the sales volume of NEV will exhibit an increasing trend in the future. The development of NEV, which includes battery electric, plug-in hybrid and hydrogen fuel-cell vehicle, was supplemented with favorable policy measures by the PRC to improve its technology and competitiveness. According to the Development Plan for the New Energy Vehicle Industry (2021-2035) (《國務院辦公廳關於印發新能源汽車產業發展規劃(2021–2035年)的通知》) (the "Plan") released by the State Council of the PRC in October 2020, development goals and targets for NEV has been set out including market size and technology advancement. According to the Plan, by 2025, it is targeted by the PRC for the NEV industry to achieve (i) key technology breakthroughs in electric battery, drivetrain, and vehicle operation systems; (ii) lower the average power consumption of pure new pure electric vehicles to 12.0 kWh/100 km; and (iii) increase NEV sales volume to 20% of total sales of new vehicles. The above encouragements can effectively stimulate market demand and supply, which is expected to boost the development of NEV market. Furthermore, with reference to the Notice on Improving the Financial Subsidy Policies for the Promotion and Application of New Energy Vehicles (《關於完善新能源汽車推廣應用財政補貼政策的通知》) jointly released by the Ministry of Finance, the Ministry of Industry and Information Technology, the Ministry of Science and Technology, and the National Development and Reform Commission in April 2020, subsidies on the NEV sales will be extended from the end of 2020 to the end of 2022, and the PRC government will improve the green car quota system to encourage automakers to make more environmentally friendly vehicles after it ends NEV subsidies in 2022 and boost NEV sales for public uses such as bus and trucks. Hence, it is anticipated that the NEV market will exhibit a strong performance growth in the future, which would in turn promote the development of the automotive parts industry.

As mentioned above, it is expected that approximately HK$480 million of the net proceeds from the Subscription will be allocated to enhance the Group's manufacturing capability in automobile products and broaden its exposure in NEV industry, which is in line with the trend of the recovery of the automobile market and the vigorous development of NEV.

Support from the Laixi government

As mentioned above, the Directors are also of the view that the Subscription represents a good opportunity for the Company to introduce a strategic investor with strong local government support. Laixi State-owned Assets Investment Center is a municipal public institution and will be interested in equity interest of the Company through its approximately 48.5% equity interest in the Subscriber upon Completion. The Subscription reflects the Laixi government's confidence in the Company's future and support for the long-term development of the Company, which is beneficial for the Company to enhance the core competitiveness of its manufacturing business. We are of the view that the Subscription may boost confidence of external investors and broaden the Shareholder base of the Company.

In addition, according to the use of proceeds from the Subscription, it is expected that approximately HK$70 million will be used for purchasing of land use rights in Laixi City for construction of new production plants to expand the Group's production capacity and technology capability for its manufacturing business. We consider that, leveraging on the Laixi government's support, the Subscription represents a valuable opportunity for the Group to expand its footprint in Shandong Province and broaden its exposure in the NEV industry.

Other fundraising alternatives

As advised by the Company, other than the Subscription, the Company considered the feasibility of other fundraising methods such as debt financing from bank or money lenders and other forms of equity financing. The Company considered that debt financing which would incur additional interest expenses would hinder the ability of the Group to achieve turnaround results in the coming years. Moreover, due to the loss-making performance of the Group and the fact that the majority of the Group's assets have already been pledged as security for the Group's existing bank borrowings, the Group could not obtain further debt financing with terms favorable to the Group. Under such circumstances, the Company considered that debt financing from banks or money lenders is not a preferable choice.

As regards equity fund-raising exercises, due to (i) the scale of the funding required; (ii) the thin trading liquidity of the Shares; and (iii) the net loss performance and high gearing position of the Group, the management of the Group expected that it would be difficult to attract investors or Shareholders to participate and appoint an underwriter to assist in any rights issue or open offer fund raising exercises. Moreover, the Company would be required to (i) undergo a relatively lengthy process to prepare and issue a prospectus and identify a suitable underwriter and share registrar; and (ii) incur additional administrative costs in respect of the rights issue or open offer, including the issuance costs of the prospectus and high underwriting fee taking into consideration the thin trading liquidity of the Shares and the Group's consecutive net loss performance and high gearing position. Taking into account the lengthy process and additional administrative costs involved, the Company considered that rights issue and open offer are also not a preferable choice.

Having considered (i) the worsening financial performance and position of the Group; (ii) the Subscription is in line with the development strategies of the Group to focus on and expand its manufacturing business; (iii) the proceeds of the Subscription will be used towards the repayment of the Group's outstanding bank loans which would alleviate the financial pressure of the Group; (iv) the prospect of the automobile industry in the PRC; (v) the support by the Laixi government through its participation in the Subscription; and (vi) it is not cost-effective nor feasible for the Group to obtain debt financing and/or carry out other forms of equity financing, we concur with the Directors' view that the Subscription offers a good opportunity to replenish working capital for the Group and to strengthen the financial position of the Company and is in the interest of the Company and the Shareholders as a whole.

2. **Principal terms of the Subscription Agreement**

Set out below is a summary of the principal terms of the Subscription Agreement.

Date

28 May 2021

Parties

(1) the Company; and

(2) the Subscriber

The Subscription Shares

Pursuant to the Subscription Agreement, the Subscriber has conditionally agreed to subscribe for, and the Company has conditionally agreed to allot and issue, a maximum of 11,252,732,911 Subscription Shares at the Subscription Price of HK$0.059 per Subscription Share and at an aggregate Subscription Price of not more than RMB554,381,000. The exact number of the Subscription Shares to be issued will be determined by dividing RMB554,381,000 to be converted into HKD at the exchange rate of the central parity rate of RMB to HKD announced by the People's Bank of China on the Business Day immediately prior to the Completion Date by the Subscription Price.

The 11,252,732,911 Subscription Shares represent approximately (i) 166.27% of the issued share capital of the Company as at the Latest Practicable Date; and (ii) 62.44% of the enlarged fully paid up issued share capital of the Company upon Completion. The maximum aggregate nominal value of the Subscription Shares is HK$1,125,273,291.1.

Ranking

The Subscription Shares will rank equally in all respects with the Shares in issue as at the date of allotment and issuance of the Subscription Shares.

Subscription Price

The Subscription Price of HK$0.059 per Subscription Share represents:

(i) a discount of approximately 47.8% to the closing price of HK$0.113 per Share as quoted on the Stock Exchange on the Latest Practicable Date;

(ii) a discount of approximately 30.6% to the closing price of HK$0.085 per Share as quoted on the Stock Exchange on 28 May 2021, being the date of the Subscription Agreement;

(iii) a discount of approximately 24.0% to the average of the closing prices of the Shares as quoted on the Stock Exchange for the five (5) consecutive trading days up to and including 27 May 2021 of approximately HK$0.0776 per Share;

(iv) a discount of approximately 25.8% to the average of the closing prices of the Shares as quoted on the Stock Exchange for the ten (10) consecutive trading days up to and including 27 May 2021 of approximately HK$0.0795 per Share; and

(v) a premium of approximately 22.9% over the audited consolidated net asset value per Share attributable to the equity Shareholders of approximately HK$0.048 as at 31 December 2020 (equivalent to approximately RMB0.04), calculated based on the Group's audited consolidated net assets attributable to the Shareholders of approximately RMB272,203,000 as at 31 December 2020 and 6,767,636,215 Shares in issue as at the Latest Practicable Date.

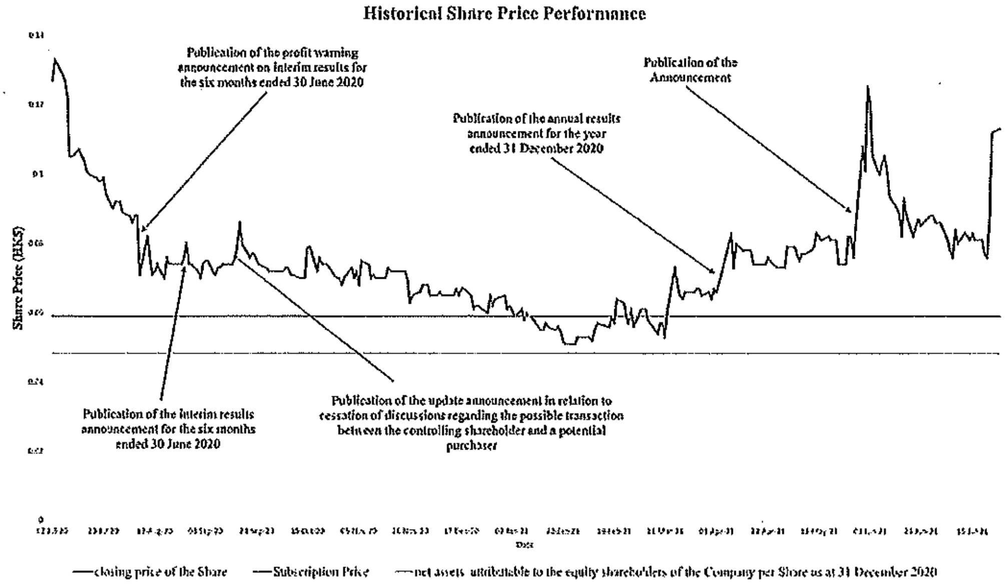
The aggregate Subscription Price shall be payable in cash in HKD by the Subscriber on Completion with reference to the exchange rate of the central parity rate of RMB to HKD announced by the People's Bank of China on the Business Day immediately prior to the Completion Date. The Subscription Price of HK$0.059 was arrived at after arm's length negotiations between the Company and the Subscriber after taking into account (i) an estimated market capitalisation of the Company of approximately HK$400 million (approximately HK$0.0591 per Share) with reference of the average of the closing prices of the Shares as quoted on the Stock Exchange for the 45 consecutive trading days up to and including 18 February 2021 of approximately HK$0.05887 per Share; (ii) the amount of the Subscription Shares to be issued; (iii) the controlling position to be obtained by the Subscriber; and (iv) the expected funding need of the Group, in particular, the substantial funding of approximately HK$480 million which will be required to build a new production plant and to acquire the related production equipment.

As it took time for the General Partner and the Limited Partners to discuss among themselves and seek internal approvals for the Subscription, the approximate Subscription Price must be agreed at the preliminary stage. Given the protracted nature of such internal processes (in particular, as one of the Limited Partners is a state-owned institution), the parties could not continuously reassess and revisit the Subscription Price based on the then prevailing closing prices of the Shares up to a date closer to the signing of the Subscription Agreement. As such, the historical 45 days average closing price up to 18 February 2021 was considered a reasonable benchmark (when compared with the average of the closing prices of the Shares as quoted on the Stock Exchange for the 30 and 60 consecutive trading days up to and including 18 February 2021, i.e. HK$0.059 and HK$0.06033 per Share, respectively) to determine the Subscription Price.

Evaluation of the Subscription Price

(i) Historical price analysis

In light of the above, we have analysed the historical closing prices of the Shares during the past twelve months prior to the Last Trading Day and up to the Latest Practicable Date. The following chart illustrates the daily closing prices of the Shares as quoted on the Stock Exchange, the Subscription Price and the net assets attributable to the equity Shareholder per Share as at 31 December 2020, during the period from 1 July 2020 up to and including the Latest Practicable Date (the "Review Period"):



Source: Stock Exchange (www.hkex.com.hk)

As shown in the chart above, the closing prices of the Shares ranged between HK$0.051 per Share and HK$0.133 per Share during the Review Period and the Shares had been traded above the net assets attributable to the equity Shareholder per Share as at 31 December 2020 of approximately HK$0.048 per Share (equivalent to approximately RMB0.04) throughout the entire Review Period.

The closing prices of the Shares surged to a peak of HK$0.133 in the first few weeks of the Review Period and started to drop thereafter and exhibited a downward trend for around eight months up to February 2021. During the first eight months, after the Company published a profit warning announcement in respect of the interim results of the Company for the six months ended 30 June 2020 ("FH2020") on 6 August 2020, the closing prices of the Shares remained stagnant at a range from HK$0.07 to HK$0.08 from August to September 2020, and further demonstrated an overall downward trend from October 2020 to February 2021 following the release of the Company's announcement dated 14 September 2020 in relation to the cessation of discussions regarding the possible transaction between the controlling shareholder and a potential purchaser involving a change in control of the controlling shareholder and indirectly a change in control of the Company. During the period from March 2021 to the Last Trading Day, the closing prices of the Shares have ramped up gradually from HK$0.061 on 1 March 2021 to HK$0.085 on the Last Trading Day, representing an increase of approximately 39.4%. After the publication of the Announcement, the closing price of the Shares reached HK$0.125 on 2 June 2021, representing the highest closing price during the period from the Last Trading Day to the Latest Practicable Date. On the Latest Practicable Date, the Shares closed at HK$0.113.

Further, the Subscription Price of HK$0.059 per Share (i) is within the range of the closing prices between HK$0.051 per Share and HK$0.133 per Share and lower than the average closing price of HK$0.075 per Share during the Review Period; (ii) represents a premium of approximately 15.7% over the lowest closing price of HK$0.051 per Share and represents a discount of approximately 55.6% to the highest closing price of HK$0.133 per Share; and (iii) represents a premium of approximately 22.9% over the net assets attributable to the equity Shareholders per Share as at the 31 December 2020.

In arriving at our opinion on the basis for determination of the Subscription Price, we observed that the financial performance and position of the Group have been worsening during FY2019 and FY2020. In particular, the total revenue from continuing operations decreased by 47.9% in FY2020, and as a result, the Group's net loss from continuing operations attributable to the Shareholders was magnified by approximately 2.9 times for FY2020. In the meanwhile, the net assets of the Group as at 31 December 2020 represented a significant decrease of approximately 68.9% as compared to the same as at 31 December 2019. Besides, we noted that, during the period starting from the publication of the profit warning announcement on the interim results of the Company for FH2020 on 6 August 2020 to the day prior to the publication of the Announcement (the "Refined Period"), the Shares generally closed within the range of approximately HK$0.05 to HK$0.08 and exhibited a declining trend after the publication of interim results announcement for FH2020. Even though the Shares started to rebound after the publication of the annual results for FY2020, the Shares generally closed within the upper bound of the range. We considered that the Subscription Price was determined with reference to the closing prices of the Shares during the Refined Period which reflected the historical financial performance of the Company.

Based on above, in spite of the fact that the historical share prices are higher than the Subscription Price at most of the time during the Review Period, after considering (i) the Group's consecutive net loss performance during FY2019 and FY2020 and its high gearing position; (ii) the Subscription Price is within the range of the closing prices of the Shares during the Refined Period; (iii) the discount represented by the Subscription Price could enhance the attractiveness of the Subscription; and (iv) the relative inactive trading condition of the Shares to be discussed below, we are of the opinion that the Subscription Price was determined on a reasonable basis.

(ii) Liquidity analysis

Set out below are the number of trading days and the percentage of the Shares' average daily trading volume as compared to the then total number of issued Shares as at the end of the period/month over the twelve-month period prior to the Latest Practicable Date:

Period/month	Total volume of the Shares traded *(Shares)*	Number of trading days *(days)*	Average daily volume (Note 1) *(Shares)*	Number of issued Shares as at the end of the period/month *(Shares)*	Approximately % of average daily trading volume to the then total number of issued Shares as at the end of the period/month (Note 2)
2020					
July	19,032,765	22	865,126	6,767,636,215	0.013%
August	88,591,820	21	4,218,658	6,767,636,215	0.062%
September	95,674,310	22	4,348,832	6,767,636,215	0.064%
October	23,349,880	18	1,297,216	6,767,636,215	0.019%
November	20,674,040	21	984,478	6,767,636,215	0.015%
December	51,756,465	22	2,352,567	6,767,636,215	0.035%
2021					
January	30,213,740	20	1,510,687	6,767,636,215	0.022%
February	43,180,800	18	2,398,933	6,767,636,215	0.035%
March	43,445,118	23	1,888,918	6,767,636,215	0.028%
April	36,860,270	19	1,940,014	6,767,636,215	0.029%
May (up to and including the Last Trading Day)	13,265,000	19	698,158	6,767,636,215	0.010%
May (31 May)	147,612,000	1	147,612,000	6,767,636,215	2.181%
June	224,970,000	21	10,712,857	6,767,636,215	0.158%
July (up to the Latest Practicable Date)	144,920,915	17	8,524,760	6,767,636,215	0.126%

Source: Stock Exchange (www.hkex.com.hk)

Notes:

1. Average daily trading volume is calculated by dividing the total trading volume of the Shares for the month/period by the number of trading days during the month/period.

2. The calculation is based on the average daily trading volume of the Shares divided by the total issued Shares at the end of each month or as at the Last Trading Day or as at the Latest Practicable Date, as applicable.

As illustrated in the table above, the average daily trading volume of the Shares has been generally thin from July 2020 to the Last Trading Day. During the period, the average daily trading volume for the respective month or period ranged from approximately 698,158 Shares to 4,348,832 Shares, representing approximately 0.010% to 0.064% of the total number of Shares in issue.

After the publication of the Announcement, on the Last Trading Day to the Latest Practicable Date, we noted that there was an increase in trading volume of the Shares. During the period, the average daily trading volume for the respective month or period ranged from approximately 8,524,760 Shares to 147,612,000 Shares, representing approximately 0.126% to 2.181% of the total number of Shares in issue.

Given the relatively low trading liquidity of the Shares prior to the publication of the Announcement, we consider that it is reasonable for the Subscription Price to be set at a discount to the average prevailing historical closing prices of the Shares. To assess the fairness and reasonableness of the level of discount implied by the Subscription Price, we further performed comparable analysis as below.

(iii) Comparable companies analysis

In order to assess the fairness and reasonableness of the Subscription Price, we have also conducted an analysis on price-to-earnings ratio (the "P/E Ratio") and price-to-book value ratio (the "P/B Ratio"), being two commonly adopted and used benchmarks for appraising the valuation of a company given the P/E Ratio takes into consideration the profitability of the subject company, while the P/B Ratio takes into account the net assets of the subject company.

In the selection of the comparable companies, our selection criteria focused on companies that (i) are listed and remain trading on the Main Board of the Stock Exchange as at the Last Trading Day; (ii) have a market capitalisation of not more than HK$1 billion (making reference to the Company's market capitalisation of approximately HK$0.5 billion as at the Last Trading Day); and (iii) are mainly engaged in the manufacturing of automotive parts and/or automobile dealership business with more than 50% of their revenue geographically derived from the PRC. According to the 2020 Annual Report, the manufacturing business (manufacturing of auto parts) and the automobile dealership and service business accounted for approximately 58.9% and 38.8% of the total revenue of the Group respectively, representing the core businesses of the Group. Based on our research on the website of the Stock Exchange in accordance with the above selection criteria, we have identified an exhaustive list of 9 companies (collectively, the "Industry Comparables"). Details of the Industry Comparables are set out below:

Comparison with the Industry Comparables

	Company name (Stock code)	Principal activities	Market Capitalisation on the Last Trading Day *HK$ million*	Latest published annual net profit/(loss) attributable to shareholders prior to the Last Trading Day *HK$ million*	Latest published net assets/ (liabilities) attributable to shareholders prior to the Last Trading Day *HK$ million*	P/E Ratio *(times)*	P/B Ratio *(times)*
1	China Automotive Interior Decoration Holdings Limited (48)	Manufacturing of automotive parts	108.7	(4.7)	211.3	N/A	0.5
2	CCT Fortis Holdings Limited (138)	Automobile dealership	170.3	(686.0)	2,138.0	N/A	0.1
3	Xinchen China Power Holdings Limited (1148)	Manufacturing of automotive parts	474.4	(970.4)	2,620.3	N/A	0.2
4	Shuanghua Holdings Limited (1241)	Manufacturing of automotive parts	61.8	(6.2)	400.0	N/A	0.2
5	China First Capital Group Limited (1269)	Manufacturing of automotive parts	256.4	(448.5)	232.0	N/A	1.1
6	Centenary United Holdings Limited (1959)	Automobile dealership	390.0	25.7	304.5	15.2	1.3
7	Ruifeng Power Group Company Limited (2025)	Manufacturing of automotive parts	800.0	40.3	1,149.9	19.8	0.7
8	Xiezhong International Holdings Limited (3663)	Manufacturing of automotive parts	608.0	(315.9)	298.5	N/A	2.0
9	China Tianrui Automotive Interiors Co., LTD. (6162)	Manufacturing of automotive parts	326.0	61.0	324.1	5.3	1.0
					Maximum	19.8	2.0
					Minimum	5.3	0.1
					Median	15.2	0.7
					Average	13.4	0.8
	The Company [(Note 1)]		339.3	(575.6)	326.6	N/A	1.2

Source: Stock Exchange (www.hkex.com.hk)

Notes:

1. The implied market capitalisation of the Company was calculated by multiplying the total issued Shares as at the Last Trading Day by the Subscription Price.

2. For the purpose of this table, conversion of RMB into HK$ in relation to the respective financial figures of the Industry Comparables and the Company denominated in RMB (if applicable and if any) is calculated at the approximate exchange rate of RMB1 to HK$1.2. This exchange rate is for illustration purpose only and does not constitute a representation that any amounts have been, could have been, or may be exchanged at this or any other rate at all.

As illustrated in the table above, the Group recorded net loss attributable to the Shareholders for FY2020, and thus the P/E ratio analysis is not applicable to the Company and the information of the Industry Comparables is thus provided for reference only. In relation to the P/B Ratio, the P/B Ratios of the Industry Comparables ranged from approximately 0.1 time to approximately 2.0 times, with a median of approximately 0.7 time and an average of approximately 0.8 time. We noted that the implied P/B Ratio of the Company is approximately 1.2 times which is within the range of the Industry Comparables, and lies above the median and the average of the Industry Comparables.

However, we noted from the above table that Industry Comparable #2, #3 and #4 recorded P/B Ratio of approximately 0.1 time, 0.2 time and 0.2 time respectively, which are substantially lower than the average of the Industry Comparables. In order to understand such extremity noted among the Industry Comparables, we perform further assessments amongst Industry Comparable #2, #3 and #4:

1. In regard to Industry Comparable #2 and in comparison to the Company, it possessed substantial investment properties portfolio amounted to approximately HK$1,645 million as at 31 December 2020, accounting for approximately 76.5% of its total equity. The substantial portion of investment properties held by Industry Comparable #2 resulted in a large asset base and hence a substantially low P/B Ratio.

2. In regard to Industry Comparable #3, during the past three years up to the Last Trading Day, its shares were generally traded between approximately HK$0.3 and HK$0.8 and there was no noticeably upward or downward trend. Based on its annual reports for past three years, its net asset attributable to its shareholders per share were approximately HK$2.79, HK$2.80 and HK$2.04 as at 31 December 2018, 2019 and 2020 respectively, reflecting that the P/B Ratio of Industry Comparable #3 amounted to 0.2 time is in line with its price trend for the past three years up to the Last Trading Day which is substantially below its net asset attributable to its shareholders.

3. In regard to Industry Comparable #4, its share price movement for the past three years since the Last Trading Day has exhibited a downward trend and dropped significantly after the release of its announcement on 10 February 2020. With reference to the announcement, the Stock Exchange considered that Industry Comparable #4 has failed to maintain a sufficient level of operations and assets of sufficient value to support its operations under Rule 13.24 of the Listing Rules, mainly taking into account that its scale of operation has substantially diminished to a low level.

Based on above our further research, in particular, (i) the significant portion of investment properties held by Industry Comparable #2 resulting in a substantially low P/B Ratio as at the Last Trading Day; and (ii) the declining trend of the historical share price of Industry Comparable #4 mainly resulting from its potential insufficient scale of operation, we consider that the inclusion of the P/B Ratios of Comparable #2 and #4 may create anomalous result and distort our assessment of the implied P/B Ratio of the Company, while we consider that Industry Comparable #3 should be remained as one of the Industry Comparables taking into account that the P/B Ratio of Industry Comparable #3 amounted to 0.2 time is in line with its price trend for the past three years up to the Last Trading Day which is substantially below its net asset attributable to its shareholders and fulfill all the selection criteria of the Industry Comparables. For illustration purpose, after removing Industry Comparable #2 and #4, the P/B Ratios of the Industry Comparables ranged from approximately 0.2 time to approximately 2.0 times with the median of approximately 1.0 time and the average of approximately 1.0 time, the implied P/B Ratio of the Company of approximately 1.2 times will still lie above the median and the average.

Conclusion on evaluation of the Subscription Price

Although the Subscription Price represents discounts of approximately 30.6%, 24.0% and 25.8% to the closing price per Share on the Last Trading Day and the average prices per Share for the period of five and 10 trading days up to and including 27 May 2021 respectively, in light of (i) the Subscription Price represents a premium of approximately 22.9% over the net assets attributable to the equity Shareholder per Share as at 31 December 2020; (ii) the Group's consecutive net loss performance during FY2019 and FY2020 and its high gearing position; (iii) the generally thin liquidity in terms of trading volume of the Shares; and (iv) the implied P/B Ratio of the Company lies above the median and the average of the Industry Comparables, we are of opinion that the Subscription Price is fair and reasonable and in the interest of the Company and Independent Shareholders as a whole from the perspective of comparable analysis.

3. Potential dilution effect on the shareholding of the Company

For illustrative purpose, set out below is the shareholding structure of the Company (i) as at the Latest Practicable Date; (ii) upon Completion (assuming there is no change in the issued share capital of the Company other than the issue of the Subscription Shares); and (iii) upon Completion assuming there is no change in the issued share capital of the Company other than the issue of the Subscription Shares and CDH has disposed of its Shares.

Shareholders	As at the Latest Practicable Date		Upon Completion (assuming a maximum of 11,252,732,911 Subscription Shares to be issued)[2]		Upon Completion (assuming a maximum of 11,252,732,911 Subscription Shares to be issued and CDH has disposed of its Shares)	
	Number of Shares	*(approximately)* %	*Number of Shares*	*(approximately)* %	*Number of Shares*	*(approximately)* %
the Subscriber and its parties acting in concert	–	–	11,252,732,911	62.44	11,252,732,911	62.44
CDH[1]	2,889,580,226	42.70	2,889,580,226	16.04	1,800,234,900	9.99[3]
Fame Mountain	1,904,761,905	28.15	1,904,761,905	10.57	1,904,761,905	10.57
Public Shareholders	1,973,294,084	29.15	1,973,294,084	10.95	3,062,639,410	17.00
Total	6,767,636,215	100.00	18,020,369,126	100.00	18,020,369,126	100.00

Notes:

1. CDH is beneficially wholly owned by CDH Fund IV, L.P. and the general partner of CDH Fund IV, L.P. is CDH IV Holdings Company Limited which is 80% beneficially owned by China Diamond Holdings IV, L.P. China Diamond Holdings Company Limited is the general partner of China Diamond Holdings IV, L.P., and China Diamond Holdings Company Limited is ultimately and beneficially owned as to (i) approximately 33.20% by Mr. Wu Shangzhi; (ii) approximately 28.78% by Mr. Jiao Shuge; (iii) approximately 7.79% by Mr. Wang Zhenyu, who is a non-executive Director; and (iv) approximately 30.23% by five Independent Third Parties, with each of them holding not more than 10% beneficial interest in China Diamond Holdings Company Limited.

2. This scenario is for illustration purpose only and will not occur, as the Subscription Shares will not be issued if the minimum public float requirement under the Listing Rules cannot be met upon Completion. As such, the Company's public float will not, in any event, fall below the prescribed minimum public float upon full issuance of the Subscription Shares.

3. CDH will become a public Shareholder upon its shareholding in the Company being decreased to less than 10% before Completion.

As shown in the table above, the public Shareholders' shareholdings (excluding CDH which will be considered as a public Shareholder immediately after Completion) will be diluted from approximately 29.15% as at the Latest Practicable Date to approximately 17.00% immediately upon the Completion and CDH has disposed of its Shares.

From the perspective of the Independent Shareholders, being the public Shareholders before Completion, even though the dilution effect on the shareholding upon Completion may be considerable, while further taking into account (i) the benefits of the Subscription as discussed under the section headed "1. Background to and reasons for the Subscription – Reasons of and benefits for the Subscription" in this letter; (ii) the worsening financial performance and position of the Group; (iii) the lack of alternative fund raising method available to the Company; (iv) the Subscription will greatly strengthen the Company's capital base and working capital position as well as the net asset position and gearing position of the Group; (v) the Subscription Price is fair and reasonable so far as the Company and the Independent Shareholders are concerned as discussed above; and (vi) the proposed use of proceeds to facilitate the Group's optimisation plan as discussed in the section "Background to and reasons for the Subscription" above, we are of the view that the Subscription is an acceptable means of fund raising by the Company and the dilution effect on the shareholding of the Independent Shareholders is acceptable so far as the Company and the Independent Shareholders are concerned.

4. Minimum public float in the Shares

CDH shall, as one of the conditions precedent to the Subscription Agreement, give an undertaking to dispose of such number of Shares before Completion so as to ensure that the minimum public float will be maintained at all times in accordance with the Listing Rules upon Completion. With reference to the Letter from the Board, the Subscriber will not waive this condition so long as there remains a possibility that the Company's public float will fall below the prescribed minimum public float requirement under the Listing Rules upon full issuance of the Subscription Shares.

It is the intention of the Board and the Subscriber that the Company will remain listed on the Stock Exchange after Completion. In addition to the undertaking from CDH as disclosed above, each of the Company and the Subscriber will undertake to the Stock Exchange to take appropriate steps to ensure that not less than 25% of the issued Shares will be held by the public. If the minimum public float requirement under the Listing Rules cannot be met upon Completion, the Subscription will not proceed.

The Company will require CDH to provide a list of purchasers/transferees/placees who will acquire the Shares held by CDH to the Company so that it can ensure those purchasers/transferees/places are Independent Third Parties before CDH's disposal prior to Completion and will designate individual(s) to be responsible for monitoring the public float position of the Company and any changes in the shareholdings of the substantial shareholders of the Company from time to time.

Based on the above, in particular (i) the undertaking by CDH to dispose certain number of Shares before Completion to maintain the minimum public float of the Company is one of the conditions precedent to the Subscription Agreement (which condition will not be waived by the Subscriber so long as there remains a possibility that the Company's public float will fall below the prescribed minimum public float requirement under the Listing Rules upon full issuance of the Subscription Shares); (ii) the Company and the Subscriber will undertake to the Stock Exchange to take appropriate steps to ensure that the Company will fulfill the minimum public float requirement; (iii) the Company will designate individual(s) to monitor the public float position of the Company from time to time; and (iv) the Subscription will not proceed if the minimum public float requirement under the Listing Rules cannot be met upon Completion, we are of the view that the Subscription Agreement is fair and reasonable and, we are of the view that the above measures and mechanism are sufficient to ensure that the Company will fulfill the public float requirement upon Completion.

5. **Possible financial effect of the Subscription**

(i) Cashflow

According to the 2020 Annual Report, the cash and cash equivalents of the Group amounted to approximately RMB64.6 million as at 31 December 2020. Upon Completion and save for the relevant expenses related to the Subscription, the cash position of the Group will be improved as the Subscription will supplement the working capital of the Group by approximately HK$62.0 million. Accordingly, the cash position, net current assets and current ratio of the Company are expected to be improved upon Completion.

(ii) Earnings

The earnings per Share is expected to decrease as the number of issued Shares will increase upon Completion. However, immediate financial burden of the Group will also be alleviated as certain borrowings of the Company will be repaid by utilising the proceeds from the Subscription. Nevertheless, Shareholders are reminded that the actual impact of the Subscription on the Company's earnings will also be dependent on the actual financial performance of the Group in the long run.

(iii) Net Asset Value

According to the 2020 Annual Report, the net assets attributable to the equity Shareholders as at 31 December 2020 was approximately RMB272.2 million. Upon Completion and save for the relevant expenses related to the Subscription, the total assets of the Group will increase. As the Subscription Price of HK$0.059 is higher than the net asset value per Share attributable to the equity Shareholders of approximately HK$0.048 as at 31 December 2020, the net asset value per Share attributable to the equity Shareholders upon Completion will increase. Accordingly, there will be a positive impact on the net assets attributable to the equity Shareholders.

(iv) Gearing

The gearing ratio of the Group as at 31 December 2020 was approximately 373.2%, as calculated by dividing total liabilities by net assets of the Group according to the 2020 Annual Report. Upon Completion and the proceeds from the Subscription being utilised as planned, the total liabilities of the Group will decrease, while the total assets of the Group will increase. Thus, the gearing level of the Group is expected to decrease.

Based on the above, the Subscription would have an overall positive effect on the future earnings and the financial position of the Group in terms of cashflow, net asset value and gearing upon Completion. On such basis, we are of the view that the Subscription is in the interests of the Company and the Shareholders as a whole.

6. The Whitewash Waiver

As at the date of the Subscription Agreement, the Subscriber and parties acting in concert with it (including the Fund, the General Partner, the Limited Partners and the Investment Manager and their respective ultimate beneficial owners) do not own or have control or direction over any Shares. Upon Completion, the Subscriber will hold a maximum of 11,252,732,911 Shares, representing approximately 62.44% of the enlarged fully paid up issued share capital of the Company. Under Rule 26.1 of the Takeovers Code, upon the allotment and issuance of the Subscription Shares at Completion, the Subscriber would be obliged to make a mandatory general offer to the Shareholders for all the issued Shares and other securities of the Company not already owned or agreed to be acquired by the Subscriber and parties acting in concert with it unless the Whitewash Waiver is granted by the Executive and the approval by 75% of the Independent Shareholders at the EGM by way of poll is obtained in accordance with the Takeovers Code.

In this regard, an application has been made to the Executive for the Whitewash Waiver in respect of the allotment and issuance of the Subscription Shares. The Whitewash Waiver, if granted by the Executive, will be subject to, among other things, the condition that respective resolutions relating to the Whitewash Waiver on one hand, and the Subscription Agreement and the grant of Specific Mandate on the other hand, being separately approved by at least 75% and more than 50%, respectively, of the votes cast by the Independent Shareholders at the EGM by way of poll. CDH shall abstain from voting at the EGM in respect of the resolution(s) approving the Subscription Agreement and the transactions contemplated thereunder as well as the Whitewash Waiver. The Whitewash Waiver is a condition precedent to the Subscription Agreement which cannot be waived. If the Whitewash Waiver is not granted by the Executive or not approved by the Independent Shareholders, the Subscription will not proceed.

Given the possible benefits of the Subscription mentioned in the section headed "1. Background to and reasons for the Subscription" above in this letter and having considered our view described above that the terms of the Subscription are fair and reasonable so far as the Independent Shareholders are concerned for the reasons set out herein, we are of the opinion that the approval for the Whitewash Waiver, which is a prerequisite of the Subscription, is in the interests of the Company and the Shareholders as a whole and is fair and reasonable for the purpose of proceeding with the Subscription.

RECOMMENDATION

Having considered the abovementioned principal factors and reasons, in particular, that:

(i) the worsening financial performance and position of the Group;

(ii) the Subscription is in line with the development strategies of the Group to focus on and expand its manufacturing business;

(iii) the proceeds of the Subscription will be used towards the repayment of the Group's outstanding bank loans which would alleviate the financial pressure of the Group;

(iv) the prospect of the auto parts and automobile industry in the PRC;

(v) the support by the Laixi government through its participation in the Subscription;

(vi) it is not cost-effective nor feasible for the Group to obtain debt financing and/or carry out other forms of equity financing;

(vii) the generally thin liquidity in terms of trading volume of the Shares;

(viii) the Subscription represents a premium of approximately 22.9% over the net assets attributable to the equity Shareholders per Share of the Company as at the 31 December 2020;

(ix) the implied P/B Ratio of the Company is higher than both of the median and the mean of the Industry Comparables; and

(x) the grant and approval of the Whitewash Waiver is a condition precedent to the completion of the Subscription Agreement,

we consider that although the entering into of the Subscription Agreement is not in the ordinary and usual course of business of the Group, the terms of the Subscription Agreement and the transactions contemplated thereunder are on normal commercial terms, the terms of the Subscription and the Whitewash Waiver are fair and reasonable so far as the Independent Shareholders are concerned, and the Subscription Agreement and the Whitewash Waiver are in the interest of the Company and the Shareholders as a whole. Accordingly, we recommend the Independent Shareholders, and advise the Independent Board Committee to recommend the Independent Shareholders, to vote in favour of the ordinary resolutions to be proposed at the EGM to approve the Subscription Agreement and the transactions contemplated thereunder and the Whitewash Waiver.

Yours faithfully,
For and on behalf of
Octal Capital Limited

Alan Fung	Louis Chan
Managing Director	*Director*

Note: Mr. Alan Fung has been a responsible officer of Type 1 (dealing in securities) and Type 6 (advising on corporate finance) regulated activities since 2003. Mr. Fung has more than 28 years of experience in corporate finance and investment banking and has participated in and completed various advisory transactions in respect of mergers and acquisitions, connected transactions and transactions subject to the compliance to the Takeovers Code of listed companies in Hong Kong.

Mr. Louis Chan has been a responsible officer of Type 1 (dealing in securities) and Type 6 (advising on corporate finance) regulated activities since 2008. Mr. Chan has more than 20 years of experience in corporate finance and investment banking and has participated in and completed various advisory transactions in respect of mergers and acquisitions, connected transactions and transactions subject to the compliance to the Takeovers Code of listed companies in Hong Kong.