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宏华集团
HONGHUA GROUP

HONGHUA GROUP LIMITED

宏華集團有限公司

(a company incorporated in the Cayman Islands with limited liability)

(Stock Code: 196)

**CONNECTED TRANSACTIONS
ENGINEERING EQUIPMENT SALES CONTRACT AND
RAW MATERIALS SALES CONTRACT**

**CONTINUING CONNECTED TRANSACTIONS
SALES FRAMEWORK AGREEMENT AND
EQUIPMENT LEASING FRAMEWORK AGREEMENT**

ENGINEERING EQUIPMENT SALES CONTRACT

On 11 December 2020, Sichuan Honghua, being a wholly-owned subsidiary of the Company, and Jiangsu Offshore entered into the Engineering Equipment Sales Contract, pursuant to which Sichuan Honghua will sell finished engineering equipment to Jiangsu Offshore with a consideration of RMB9,153,549.46.

RAW MATERIALS SALES CONTRACT

On 11 December 2020, Sichuan Honghua and Jiangsu Offshore entered into the Raw Materials Sales Contract, pursuant to which Sichuan Honghua will sell raw materials including steel sheets and steel pipes to Jiangsu Offshore with a consideration of RMB2,474,217.62.

SALES FRAMEWORK AGREEMENT

On 11 December 2020, Sichuan Honghua and Jiangsu Offshore entered into the Sales Framework Agreement with a term commencing on 1 January 2021 and expiring on 31

December 2021, pursuant to which Sichuan Honghua and its associates will sell finished products including equipment, parts, components or raw materials and engineering equipment and other related or similar goods and provide technical testing and related services to Jiangsu Offshore and its associates.

EQUIPMENT LEASING FRAMEWORK AGREEMENT

On 11 December 2020, Sichuan Honghua and Jiangsu Offshore entered into the Equipment Leasing Framework Agreement with a term commencing on 1 January 2021 and expiring on 31 December 2021, pursuant to which Sichuan Honghua and its associates will lease general equipment related to production and operation, such as transportation equipment, production equipment, construction machinery and instrument meters to Jiangsu Offshore and its associates.

LISTING RULES IMPLICATIONS

As at the date of this announcement, Jiangsu Offshore is owned as to 51% equity interest by Jiangsu Hongjieding and as to 49% indirectly by the Company. Mr. Zhang Mi, an executive Director of the Company, through his sole proprietorship, holds 53.85% equity interests in Jiangsu Hongjieding as of the date of this announcement. Accordingly, Jiangsu Offshore is a connected person of the Company, and the transactions under the Engineering Equipment Sales Contract, the Raw Materials Sales Contract, the Sales Framework Agreement and the Equipment Leasing Framework Agreement constitute connected transactions of the Company under Chapter 14A of the Listing Rules.

In respect of the Engineering Equipment Sales Contract and the Raw Materials Sales Contract, as one or more of the applicable percentage ratios calculated on an aggregated basis under Rule 14A.81 of the Listing Rules exceed 0.1% but less than 5%, the Engineering Equipment Sales Contract, the Raw Materials Sales Contract and the transactions contemplated thereunder are subject to the reporting and announcement requirements but are exempt from the Independent Shareholders' approval requirement under Chapter 14A of the Listing Rules.

In respect of the Sales Framework Agreement, as one or more of the applicable percentage ratios set out in the Listing Rules exceed 0.1% but are less than 5%, the Sales Framework Agreement and the annual cap of the transactions contemplated thereunder are subject to the reporting, announcement and annual review requirements but are exempt from the Independent Shareholders' approval requirement under Chapter 14A of the Listing Rules.

In respect of the Equipment Leasing Framework Agreement, as one or more of the applicable

percentage ratios set out in the Listing Rules exceed 0.1% but are less than 5%, the Equipment Leasing Framework Agreement and the annual cap of the transactions contemplated thereunder are subject to the reporting, announcement and annual review requirements but are exempt from the Independent Shareholders' approval requirement under Chapter 14A of the Listing Rules.

I • THE SALES TRANSACTIONS

On 11 December 2020, Sichuan Honghua, being a wholly-owned subsidiary of the Company, and Jiangsu Offshore entered into the Engineering Equipment Sales Contract, the Raw Materials Sales Contract and the Sales Framework Agreement respectively, pursuant to which Sichuan Honghua and its associates will sell certain products and services to Jiangsu Offshore and its associates, details of which are as follows.

1. Engineering Equipment Sales Contract

Date:

11 December 2020

Parties:

- (1) Sichuan Honghua
- (2) Jiangsu Offshore

Subject matter:

Pursuant to the Engineering Equipment Sales Contract, Sichuan Honghua will sell finished engineering equipment to Jiangsu Offshore.

Consideration and payment:

The consideration under the Engineering Equipment Sales Contract is RMB 9,153,549.46. The consideration was determined after arm's length negotiations between the parties with reference to the costs, reasonable profit margins and market conditions of the products and services.

After Sichuan Honghua delivers the products that meet the requirements of the Engineering Equipment Sales Contract and the VAT invoice of the full amount is received, Jiangsu Offshore shall pay 100% of the total consideration under the Engineering Equipment Sales Contract payable to Sichuan Honghua within 60 days from the date when the final acceptance report is issued.

2. Raw Materials Sales Contract

Date:

11 December 2020

Parties:

- (1) Sichuan Honghua
- (2) Jiangsu Offshore

Subject matter:

Pursuant to the Raw Materials Sales Contract, Sichuan Honghua will sell raw materials including steel sheets and steel pipes to Jiangsu Offshore.

Consideration and payment:

The consideration under the Raw Materials Sales Contract is RMB2,474,217.62. The consideration was determined with reference to the market prices of the relevant raw materials after arm's length negotiations between the parties.

After Sichuan Honghua delivers the products that meet the requirements of the Raw Materials Sales Contract, Jiangsu Offshore shall pay 100% of the total consideration under the Raw Materials Sales Contract payable to Sichuan Honghua within 30 days from the date when the final acceptance report is issued.

3. Sales Framework Agreement

Date:

11 December 2020

Parties:

- (1) Sichuan Honghua (on behalf of itself and its associates)
- (2) Jiangsu Offshore (on behalf of itself and its associates)

Subject matter:

Pursuant to the Sales Framework Agreement, Sichuan Honghua and its associates will sell equipment, parts, components or raw materials, finished products and other related or similar goods and provide technical testing and related services (hereinafter collectively referred to as the “**Products and Services**”) to Jiangsu Offshore and its associates.

Term of agreement:

The term of the Sales Framework Agreement will commence on 1 January 2021 and expire on 31 December 2021.

Pricing policy:

The prices and terms for the provision of the Products and Services by Sichuan Honghua and its associates to Jiangsu Offshore and its associates shall be determined based on the following principles:

- (i) where there are market prices for the relevant Products and Services, the prices shall be determined with reference to the prevailing market prices, being the prices at which the same type of Products and Services are provided by the Group to at least two independent third party customers on normal commercial terms; and
- (ii) where there are no market prices for the relevant Products and Services which meet the specific business needs of Jiangsu Offshore and its associates, the prices shall be determined with reference to the costs, reasonable profit margins and market conditions of the Products and Services. Such prices shall be fair and reasonable and on normal commercial terms. The mark-up rate charged by Sichuan Honghua and its associate for all transactions shall not be lower than 10%. The prices provided by Sichuan Honghua and its associates to Jiangsu Offshore and its associates shall be no less favourable to Sichuan Honghua and its associates than those provided by them to the independent third parties.

Information for historical transactions:

The following table sets out the historical amount of the sales of the Products and Services by Sichuan Honghua and its associates to Jiangsu Offshore and its associates for the three years ended 31 December 2019 and the ten months ended 31 October 2020:

Unit: RMB

	For the year ended 31 December 2017	For the year ended 31 December 2018	For the year ended 31 December 2019	For the ten months ended 31 October 2020
Products and Services	93,412,541.50	1,466,178.80	1,844,309.00	379,018.00

Annual cap and basis of determination:

The annual cap under the Sales Framework Agreement for the year ended 31 December 2021 is RMB 20 million.

The annual cap of the Sales Framework Agreement was determined based on the following factors:

- (i) the historical transactions between Sichuan Honghua and its associates and Jiangsu Offshore and its associates;
- (ii) the tentative cooperation projects of Jiangsu Offshore and its associates with Sichuan Honghua and its associates, the progress of project delivery, and their expected procurement needs in respect of the relevant Products and Services during the term of the Sales Framework Agreement; and
- (iii) the costs of the relevant Products and Services provided by Sichuan Honghua and its associates.

4. Reasons for and benefits of the Sales Transactions

The Group and Jiangsu Offshore and its associates have a good foundation for cooperation in offshore wind power projects, especially in steel structure processing and construction. Due to the production needs of the cooperation projects, Jiangsu Offshore and its associates need to purchase a large number of products and services including raw materials and engineering equipment related to the projects. The Group currently possesses inventory of the relevant products and sufficient technical services, which can meet the needs of the projects of Jiangsu Offshore and its associates. Entering into the Engineering Equipment Sales Contract, the Raw Materials Sales Contract and the Sales Framework Agreement is in line with the business development needs of the Group, and is beneficial for clearing the product inventory backlog and selling relevant technical services as well as achieving full synergic effect between the Group and Jiangsu Offshore and its associates under fair and reasonable circumstances.

The Company will retain the flexibility and discretion to select purchasers among Jiangsu Offshore and its associates and other independent third parties based on arm's length negotiations after taking into consideration commercial terms and other factors.

The Directors, including the independent non-executive Directors, are of the view that the Sales Transactions are carried out in the ordinary course of business of the Group, on normal commercial terms which are fair and reasonable, and in the interest of the Company and the Shareholders as a whole.

II. EQUIPMENT LEASING FRAMEWORK AGREEMENT

On 11 December 2020, Sichuan Honghua and Jiangsu Offshore entered into the Equipment Leasing Framework Agreement, pursuant to which Sichuan Honghua and its associates will lease general equipment related to production and operation, such as transportation equipment, production equipment, construction machinery and instrument meters (hereinafter collectively referred to as the "**Leasing Equipment**") to Jiangsu Offshore and its associates.

Parties:

- (1) Sichuan Honghua (on behalf of itself and its associates)
- (2) Jiangsu Offshore (on behalf of itself and its associates)

Subject matter:

Pursuant to the Equipment Leasing Framework Agreement, Sichuan Honghua and its associates will lease the Leasing Equipment to Jiangsu Offshore and its associates.

Term of agreement:

The term of the Equipment Leasing Framework Agreement will commence on 1 January 2021 and expire on 31 December 2021.

Pricing policy:

The prices and terms for the leasing of the Leasing Equipment by Sichuan Honghua and its associates to Jiangsu Offshore and its associates shall be determined based on the following principles:

(i) the prices shall be determined with reference to local comparable market prices, being the prices at which the Group leases the same type of equipment to at least two independent third party customers on normal commercial terms;

(ii) if comparable market prices are not available, the prices shall be determined via appraisal by a professional appraisal agency plus the costs and expenses not included in the scope of appraisal; and

If items (i) and (ii) are not applicable, the prices will be determined through negotiations taking into account the depreciation of equipment, management fees, relevant taxes (VAT and surcharges) and reasonable profit. The mark-up rate charged by Sichuan Honghua and its associates for all transactions shall normally not be lower than 10%.

The rental for specific lease transactions shall be provided for in the specific lease agreements to be entered into by the parties or their associates separately. The pricing mechanism and the transaction terms for the leasing of the Leasing Equipment by Sichuan Honghua and its associates to Jiangsu Offshore and its associates shall be fair and reasonable, on normal commercial terms, and no less favourable to Sichuan Honghua and its associates than the terms provided by them to the independent third parties.

Information for historical transactions:

The following table sets out the historical amount of the leasing of the Leasing Equipment by Sichuan Honghua and its associates to Jiangsu Offshore and its associates for the three years ended 31 December 2019 and the ten months ended 31 October 2020:

				<i>Unit: RMB</i>
	For the year ended 31 December 2017	For the year ended 31 December 2018	For the year ended 31 December 2019	For the ten months ended 31 October 2020

Leasing Equipment	0	0	0	100,000
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Annual cap and basis of determination:

The annual cap under the Equipment Leasing Framework Agreement for the year ended 31 December 2021 is RMB10 million.

The annual cap of the Equipment Leasing Framework Agreement was determined based on the following factors:

- (i) the demands of Jiangsu Offshore and its associates for leasing external equipment in order to meet their production requirements, and the type and scale of such equipment; and
- (ii) the estimated lease term, costs and calculation of lease prices of the Leasing Equipment.

Reasons for and benefits of the Equipment Leasing Transactions:

For project conducting purposes, Jiangsu Offshore and its associates need to externally purchase or lease general equipment such as transportation equipment, production equipment, construction machinery and instrument meters. The Group currently possesses a large number of the relevant equipment, which can meet the needs of the project of Jiangsu Offshore and its associates. Carrying out the Equipment Leasing Transactions will revitalize and utilize idle resources of the Group, thereby achieving full synergic effect between the Group and Jiangsu Offshore and its associates and achieving a win-win situation.

The Directors, including the independent non-executive Directors, are of the view that the Equipment Leasing Transactions are carried out in the ordinary course of business of the Group, on normal commercial terms which are fair and reasonable, and in the interest of the Company and the Shareholders as a whole.

III. INTERNAL CONTROL

The Company has formulated a number of measures and policies, including connected transaction administrative measures and management measures, to ensure that all connected transactions of the Company are effectively controlled and monitored. The Group will, through its internal control procedures and a series of risk management arrangements in accordance with the regulatory requirements, endeavour to maintain its independence in decision-making as well as the fairness of the prices and terms of each continuing connected transaction. Such arrangements include:

- (i) each continuing connected transaction contemplated under the Sales Framework Agreement and the Equipment Leasing Framework Agreement shall be conducted on a non-exclusive basis. The

Group has the flexibility to enter into arrangements with independent third parties for selling or leasing equipment, products and/or services as it deems fit;

- (ii) the pricing mechanism is transparent and the implementation of such pricing mechanism is subject to strict scrutiny by the finance department, technical department, internal audit department and the legal department of the Company. This will ensure that the transactions are conducted in accordance with the relevant pricing policies and the quotations obtained meet the specification requirements;
- (iii) with regard to the Sales Framework Agreement, before the respective subsidiary of the Company enters into any transaction according to the Sales Framework Agreement, the relevant sales department will collect the information of purchasers (as the case may be) for purchaser selection, arrange the legal department, finance department, technical department, production department, quality department and other relevant departments to review the contracts, subject to evaluation, review and approval by the chairman's office of the respective subsidiary to ensure the relevant terms and pricing are arrived at on a fair and reasonable basis;
- (iv) with regard to the Equipment Leasing Framework Agreement, before the respective subsidiary of the Company enters into any transaction according to the Equipment Leasing Framework Agreement, the relevant asset management department will negotiate the terms of quotations with the equipment leasing demanders (if necessary, an asset appraisal of the equipment to be leased out for quotation purpose will be conducted pursuant to the relevant requirements of the asset valuation and management measures of the Company). After taking into account factors such as price quotations, equipment status, particular needs of the parties to the transactions and performance capability, etc., the asset management department of the respective subsidiary will make a proposal to the chairman's office for determining the equipment leasing demanders.
- (v) the legal and securities department and the finance department of the Company will monitor the continuing connected transactions, and the relevant departments shall report to the legal and securities department and the finance department monthly on the implementation of the continuing connected transactions, to ensure that the transactions have been or will be carried out in accordance with the relevant pricing policies or mechanisms;
- (vi) the auditors and audit committee of the Company will also conduct annual review of the continuing connected transactions to confirm whether the continuing connected transactions have been conducted in compliance of the pricing policies or mechanisms and whether the relevant annual caps have been exceeded.

By implementing the above procedures and internal control measures, the Directors consider that the Company has established sufficient internal control measures to ensure the pricing basis of transactions contemplated under the Sales Framework Agreement and the Equipment Leasing Framework Agreement will be on market terms and on normal commercial terms and will be fair and reasonable to the Company and its Shareholder(s) as a whole.

IV. LISTING RULES IMPLICATIONS

As at the date of this announcement, Jiangsu Offshore is owned as to 51% equity interest by Jiangsu Hongjieding and as to 49% indirectly by the Company. Mr. Zhang Mi, an executive Director of the Company, through his sole proprietorship, holds 53.85% equity interests in Jiangsu Hongjieding as of the date of this announcement. Accordingly, Jiangsu Offshore is a connected person of the Company, and the transactions under the Engineering Equipment Sales Contract, the Raw Material Sales Contract, the Sales Framework Agreement and the Equipment Leasing Framework Agreement constitute connected transactions of the Company under Chapter 14A of the Listing Rules.

In respect of the Engineering Equipment Sales Contract and the Raw Materials Sales Contract, as one or more of the applicable percentage ratios calculated on an aggregated basis under Rule 14A.81 of the Listing Rules exceed 0.1% but less than 5%, the Engineering Equipment Sales Contract, the Raw Materials Sales Contract and the transactions contemplated thereunder are subject to the reporting and announcement requirements but are exempt from the Independent Shareholders' approval requirement under Chapter 14A of the Listing Rules.

In respect of the Sales Framework Agreement, as one or more of the applicable percentage ratios set out in the Listing Rules exceed 0.1% but are less than 5%, the Sales Framework Agreement and the annual cap of the transactions contemplated thereunder are subject to the reporting, announcement and annual review requirements but are exempt from the Independent Shareholders' approval requirement under Chapter 14A of the Listing Rules.

In respect of the Equipment Leasing Framework Agreement, as one or more of the applicable percentage ratios set out in the Listing Rules exceed 0.1% but are less than 5%, the Equipment Leasing Framework Agreement and the annual cap of the transactions contemplated thereunder are subject to the reporting, announcement and annual review requirements but are exempt from the Independent Shareholders' approval requirement under Chapter 14A of the Listing Rules.

Mr. Zhang Mi, an executive Director of the Company, is deemed to be interested in the Engineering Equipment Sales Contract, the Raw Material Sales Contract, the Sales Framework Agreement and the Equipment Leasing Framework Agreement and therefore has abstained from voting at the relevant Board meeting on resolutions in respect of the Engineering Equipment Sales Contract, the Raw Material Sales Contract, the Sales Framework Agreement and the Equipment Leasing Framework Agreement.

V. GENERAL INFORMATION

The Group is principally engaged in the business of developing, manufacturing and selling drilling rigs, rig parts and components and providing after-sales services. Sichuan Honghua, a company incorporated in the PRC, is principally engaged in the research, design, manufacturing and service of drilling and exploiting equipment, the general contracting of petrochemical engineering, the general contracting of construction engineering and the contracting of steel structure engineering. As at the date of this announcement, Sichuan Honghua is a wholly-owned subsidiary of the Company.

Jiangsu Offshore, a company incorporated in the PRC and ultimately controlled by Mr. Zhang Mi, an executive Director of the Company, is principally engaged in offshore oil and gas engineering, and the research and development, design, manufacturing, sales and maintenance of the vessels and large-scale steel structure construction.

VI. DEFINITIONS

In this announcement, unless the context otherwise requires, the following terms have the following meanings:

“associate(s)”	has the same meaning ascribed to it under the Listing Rules;
“Board”	the board of Directors;
“Company”	Honghua Group Limited, a company incorporated in the Cayman Islands with limited liability, the Shares of which are listed on the Main Board of the Stock Exchange;
“connected person(s)”	has the same meaning ascribed to it under the Listing Rules;
“Director(s)”	the director(s) of the Company;
“Engineering Equipment	the finished engineering equipment sales contract dated

Sales Contract”	11 December 2020 entered into between Sichuan Honghua and Jiangsu Offshore;
“Equipment Leasing Framework Agreement”	the equipment leasing framework agreement dated 11 December 2020 entered into between Sichuan Honghua and Jiangsu Offshore;
“Equipment Leasing Transactions”	the transactions contemplated under the Equipment Leasing Framework Agreement;
“Group”	the Company and its subsidiaries;
“Hong Kong”	the Hong Kong Special Administration Region of the People’s Republic of China;
“Independent Shareholder(s)”	Shareholder(s) other than Zhang Mi and his associates;
“Jiangsu Hongjieding”	Jiangsu Hongjieding Energy Technology Co., Ltd. (江蘇宏捷鼎能源科技有限公司), a limited liability company incorporated in the PRC;
“Listing Rules”	the Rules Governing the Listing of Securities on the Stock Exchange;
“Main Board”	the stock market operated by the Stock Exchange, excluding GEM;
“PRC”	the People’s Republic of China;
“Raw Materials Sales Contract”	the raw materials sales contract dated 11 December 2020 entered into between Sichuan Honghua and Jiangsu Offshore;
“RMB”	Renminbi, the lawful currency of the PRC;
“Sales Framework Agreement”	the sales framework agreement dated 11 December 2020 entered into between Sichuan Honghua and Jiangsu Offshore;
“Sales Transactions”	the transactions contemplated under the Engineering Equipment Sales Contract, the Raw Material Sales Contract and the Sales Framework Agreement;
“Jiangsu Offshore”	Honghua Offshore Oil & Gas Equipment (Jiangsu) Co., Ltd. (宏華海洋油氣裝備(江蘇)有限公司), a limited liability company incorporated in the PRC;
“Share(s)”	ordinary share(s) of HK\$0.1 each in the capital of the Company;

“Shareholder(s)”	holder(s) of ordinary share(s) of HK\$0.1 each in the capital of the Company;
“Sichuan Honghua”	Sichuan Honghua Petroleum Equipment Co., Ltd. (四川宏華石油設備有限公司), a company incorporated in the PRC with limited liability, and a wholly-owned subsidiary of the Company;
“Stock Exchange”	The Stock Exchange of Hong Kong Limited; and
“%”	per cent.

By order of the Board
Honghua Group Limited
Jin Liliang
Chairman

PRC, 11 December 2020

As at the date of this announcement, the executive directors of the Company are Mr. Jin Liliang (Chairman), Mr. Zhang Mi and Mr. Ren Jie; the non-executive directors of the Company are Mr. Han Guangrong and Mr. Chen Wenle; and the independent non-executive directors of the Company are Mr. Liu Xiaofeng, Mr. Chen Guoming, Ms. Su Mei, Mr. Poon Chiu Kwok, Mr. Chang Qing and Mr. Wei Bin.