



SOMERLEY CAPITAL LIMITED

20/F., China Building, 29 Queen's Road Central, Hong Kong

Telephone: 2869 9090 Fax: 2526 2032 E-Mail: somerley@somerley.com.hk

16 June 2022

To: *the independent board committee and the independent shareholders*

Dear Sirs,

MAJOR AND CONNECTED TRANSACTION INVOLVING PROPOSED ACQUISITION OF VESSELS

INTRODUCTION

We refer to our appointment as the independent financial adviser to advise the independent board committee and the independent shareholders of CSSC (Hong Kong) Shipping Company Limited (the “**Company**”) in relation to the acquisition of vessels from Wuchang Shipbuilding Industry Group Co., Ltd. (the “**Proposed Acquisition**”). Details of the Proposed Acquisition are set out in the “Letter from the Board” (the “**Board Letter**”) contained in the circular of the Company dated 16 June 2022 (the “**Circular**”), of which this letter forms part. Capitalised terms used in this letter shall have the same meanings as those defined in the Circular unless otherwise defined herein.

CA Shipping (being an indirect non-wholly owned subsidiary of the Company) or its nominees entered into the Proposed Acquisition to acquire the Vessels at a consideration of US\$91.92 million (equivalent to approximately HK\$716.98 million) from Wuchang Shipbuilding (being an indirect wholly-owned subsidiary of China Shipbuilding Group).

According to the Board Letter, as at the Latest Practicable Date, China Shipbuilding Group (through CSSC Group) is interested in approximately 75% of the issued share capital of the Company and is the indirect shareholder of Wuchang Shipbuilding. Wuchang Shipbuilding is a connected person of the Company. The Proposed Acquisition constitutes a major and connected transaction of the Company and is subject to the reporting, announcement, circular and the Independent Shareholders’ approval requirements under Chapter 14 and Chapter 14A of the Listing Rules.



The Independent Board Committee comprising all the independent non-executive Directors, namely Mr. Wang Dennis, Mdm. Shing Mo Han Yvonne and Mr. Li Hongi, has been established to advise the Independent Shareholders in relation to the Proposed Acquisition. We, Somerley Capital Limited, have been appointed as the Independent Financial Adviser to advise the Independent Board Committee and the Independent Shareholders in this regard.

During the past two years, Somerley Capital Limited has acted as the independent financial adviser to the independent board committee and independent shareholders of the Company in relation to notifiable and connected transactions involving acquisition of vessels (details of which are set out in the Company's circular dated 31 January 2022). Such past engagement was limited to providing independent advisory services to the independent board committee and independent shareholders of the Company pursuant to the Listing Rules. Under the past engagement, Somerley Capital Limited received normal professional fees from the Company. Given the independent advisory nature of the past engagements, as at the Latest Practicable Date, there were no relationships or interests between (a) Somerley Capital Limited and (b) the Group and Wuchang Shipbuilding that could reasonably be regarded as a hindrance to our independence as defined under Rule 13.84 of the Listing Rules to act as the independent financial adviser to the Independent Board Committee and the Independent Shareholders with respect to the matters set out above.

In formulating our opinion, we have relied on the information as contained in the Circular and the information and facts supplied, and the opinions expressed, by the Directors and management of the Company (the "**Management**"). We have assumed that the information and facts provided and opinions expressed to us are true, accurate and complete in all material aspects. We have also sought and received confirmation from the Directors that all material relevant information has been supplied to us and that no material facts have been omitted from the information supplied and opinions expressed to us. We have no reason to doubt the truth or accuracy of the information provided to us, or to believe that any material information has been omitted or withheld. We have relied on such information and consider that the information we have received is sufficient for us to reach our advice and recommendation as set out in this letter. However, we have not conducted any independent investigation into the business and affairs of the Group or Wuchang Shipbuilding, nor have we carried out any independent verification of the information supplied.



PRINCIPAL FACTORS AND REASONS CONSIDERED

In arriving at our opinion with respect to the Proposed Acquisition, we have taken into account the principal factors and reasons set out below.

1. Information on the parties to the Proposed Acquisition

The Group

The Company is a shipyard-affiliated leasing company and is principally engaged in the provision of leasing services.

CA Shipping is a joint venture established by Fortune Vcontainer Carriers and ASL NAVIGATION. CA Shipping is an indirect non-wholly owned subsidiary of the Company and its financial results will be consolidated into the financial statements of the Group.

Fortune Vcontainer Carriers is a company established in Hong Kong with limited liability and a wholly-owned subsidiary of the Company, which is principally engaged in the provision of leasing services. ASL NAVIGATION is a company incorporated in Hong Kong with limited liability and is principally engaged in shipping business. As at the Latest Practicable Date, ASL NAVIGATION is wholly-owned by ASL Shipping Limited (“**ASL Shipping**”). As set out in the Board Letter, to the best knowledge, information and belief of the Directors and having made all reasonable enquiries, as at the Latest Practicable Date, ASL Shipping is ultimately owned as to approximately 55% by Hsing Tai-Ming and as to approximately 45% by Yang Xiangdong, respectively. ASL NAVIGATION, ASL Shipping and its ultimate beneficial owners are Independent Third Party.

The original buyer under novation arrangement

The Proposed Acquisition involves the novation of agreements originally entered into between Wuchang Shipbuilding, being the shipbuilder, and ASL Shipping, being the original buyer. ASL Shipping is principally engaged in shipping business.

Wuchang Shipbuilding (the shipbuilder)

Wuchang Shipbuilding is a company incorporated under the laws of the PRC and is principally engaged in shipbuilding business. It is an indirect wholly-owned subsidiary of China Shipbuilding Group, the sole shareholder of CSSC Group and one of the controlling shareholders of the Company.



2. Reasons for and benefits of the Proposed Acquisition

As advised by the Management, CSSC Group is a leading state-owned shipbuilding conglomerate in the PRC. CSSC Group has solid experience and substantial expertise in shipbuilding and is equipped with capabilities in constructing a wide range of vessels. The Group is principally engaged in the provision of operating lease and financial lease. During the ordinary and usual course of business of the Group, the Group has been purchasing vessels from CSSC Group and/or its associates (either through entering into direct shipbuilding contract with the shipbuilders or novation of shipbuilding contracts previously entered into between the Group's lessee customers and the shipbuilders) since its establishment in 2012. The vessels purchased from CSSC Group and/or its associates have been used for the Group's operating lease business and for direct finance lease transactions (both being the Group's principal businesses). When the vessels purchased under the Proposed Acquisition are delivered from the shipbuilder, the Group would be able to generate leasing income by leasing the vessels to customer(s).

To understand the shipping market, we have performed an analysis on the ClarkSea Index, a weighted average index of earnings for the main vessel types where the weighting is based on the number of vessels in each fleet sector created by the Clarkson Research Services Limited ("Clarkson"). Clarkson is the research arm of Clarkson Plc (<https://www.clarksons.com/>), an international provider of integrated shipping services. Since the listing of the Company on the Stock Exchange on 17 June 2019, the average ClarkSea Index increased from approximately US\$13,050/day in June 2019 to approximately US\$40,651/day in March 2022. The ClarkSea Index remained stable from 2019 to 2020, with an average of approximately US\$15,082/day in 2019 and an average of approximately US\$14,839/day in 2020. The average ClarkSea Index then increased to approximately US\$28,700/day in 2021 and approximately US\$35,118/day during January to March 2022. The ClarkSea Index increased significantly since 2021, from approximately US\$15,386/day in January 2021 to approximately US\$40,651/day in March 2022. The shipping industry was on a positive trend recently based on the statistics above.

The Management considers that CSSC Group together with its associates have consistently delivered quality vessels to the Group in a timely manner. In this regard, we obtained from the Company copies of protocol of delivery and acceptance (being documents executed by the shipbuilders and buyers upon delivery of vessels) of certain previous vessels (being the delivered vessels during the year ended 31 December 2021 pursuant to shipbuilding contracts between the Company and CSSC Group and/or its associates which were effective since the Company's listing on the Stock Exchange) acquired from CSSC Group and/or its associates. We noted that the delivery time of these vessels (i.e. the date of the protocol of delivery and acceptance) is within the permitted delivery schedule according to the terms of relevant shipbuilding contracts, and the Management also confirmed that there has not been any material breach of contractual terms of the agreements on the part of CSSC Group and/or its associates. The Management considers that the transactions between the Group and CSSC Group are conducted under fair and reasonable terms, and the vessels supplied by CSSC Group enable the Group to maintain stable business operation.



As advised by the Management, it is the Group's strategy to continue strengthening its fleet size so as to expand its business. According to the Company's 2021 annual report, the Group will continue to maintain continuous investment in new ship leasing assets. With reference to the Company's 2020 annual report and 2021 annual report, the Group' fleet size increased from 136 vessels (90 of which were chartered for operation and 46 of which were under construction) as at 31 December 2020 to 158 vessels (130 of which were under lease and 28 of which were under construction) as at 31 December 2021. As further mentioned in the Company's 2021 annual report, the audited net profit of the Group for the year ended 31 December 2021 increased by approximately 24.6% as compared to that of 2020. As advised by the Management, such increase in profit was mainly attributable to, among other things, (i) the substantial increase of demand of the Group's self-operating bulk carrier fleet; and (ii) the growth of the Group's operating fleet, which is up to 130 vessels as of 31 December 2021, representing an increase of approximately 44.4% from 90 vessels as of 31 December 2020. In light of the above, we consider that the Proposed Acquisition is in line with the Group's development strategy to continue strengthening its fleet size. We are also of the view that the Group's strategy to continue strengthening its fleet size is in the interests of the Company and the Shareholders as a whole having considered (i) that the Group conducts operating and finance lease of vessels as its principal business, the acquisition/construction of vessels is prerequisite to the Group's ordinary business operation; and (ii) the recent positive industry trend as mentioned above.

Taking into account that (i) the Proposed Acquisition is in line with the Group's principal business (as the vessels purchased will be used for the Group's operating lease business and/or for direct finance lease transactions); (ii) when the vessels purchased under the Proposed Acquisition are delivered from the shipbuilder, the Group would be able to generate leasing income by leasing the vessels to customer(s); (iii) the Group has been purchasing vessels from CSSC Group and/or its associates over the past years; and (iv) the Proposed Acquisition is in line with the Group's development strategy to continue strengthening its fleet size, we concur with the Management's view that the Proposed Acquisition is in the interests of the Company and the Shareholders as a whole and is in the ordinary and usual course of business of the Group.



3. Principal terms of the Proposed Acquisition

Set out below is a summary of principal terms of the Proposed Acquisition, details of which are set out in the Board Letter.

On 31 March 2022, ASL Shipping entered into two shipbuilding contracts (the “**Initial Shipbuilding Contract I**” and the “**Initial Shipbuilding Contract II**”, and collectively, the “**Initial Shipbuilding Contracts**”) with Wuchang Shipbuilding in relation to the acquisition of two Vessels at the consideration of US\$22.88 million each. The principal terms of the Initial Shipbuilding Contracts are substantially identical, except for the delivery dates and certain terms for delay in delivery. On 27 May 2022, ASL Shipping entered into two addendums (the “**Initial Shipbuilding Contract Addendums**”) with Wuchang Shipbuilding pursuant to which the consideration for the acquisition of Vessel shall be adjusted to US\$22.98 million, taking into account the extra costs of Vessel construction. Other than the aforesaid adjustment to consideration, the other terms of the Initial Shipbuilding Contracts shall remain unchanged.

On 27 May 2022, CA Shipping (being an indirect non-wholly owned subsidiary of the Company) entered into two novation agreements with Wuchang Shipbuilding (being a subsidiary of CSSC Group) and ASL Shipping pursuant to which, among other things, all rights and obligations of ASL Shipping under the Initial Shipbuilding Contracts (as supplemented by the Initial Shipbuilding Contract Addendums) shall be assumed by CA Shipping or its nominees.

On 27 May 2022, CA Shipping entered into two shipbuilding contracts (the “**New Shipbuilding Contract I**” and the “**New Shipbuilding Contract II**”, and collectively, the “**New Shipbuilding Contracts**”) with Wuchang Shipbuilding in relation to the acquisition of two Vessels at the consideration of US\$22.88 million each. The principal terms of the New Shipbuilding Contract I and the New Shipbuilding Contract II are substantially identical as the Initial Shipbuilding Contract I and the Initial Shipbuilding Contract II respectively, except for the buyer and the delivery dates. On 13 June 2022, CA Shipping entered into two addendums with Wuchang Shipbuilding pursuant to which the consideration for the acquisition of Vessel shall be adjusted to US\$22.98 million, taking into account the extra costs of Vessel construction. Other than the aforesaid adjustment to consideration, the other terms of the New Shipbuilding Contracts shall remain unchanged.

Vessels to be acquired

The Vessels, being four 1,100 TEU container vessels

According to the Board Letter, it is currently expected that the Vessels will be delivered between 31 January 2024 to 31 August 2024.



Consideration

The consideration of one Vessel is US\$22.98 and the total consideration of the Vessels is US\$91.92 million (equivalent to approximately HK\$716.98 million) (the “**Consideration**”) and shall be settled in following agreed milestones of the shipbuilding progress of the Vessels:

- (a) a sum equivalent to 20% of the Consideration shall be paid by CA Shipping to Wuchang Shipbuilding within five banking days after the buyer’s receipt of refund guarantee by the shipbuilder;
- (b) a sum equivalent to 10% of the Consideration shall be paid by CA Shipping to Wuchang Shipbuilding upon steel cutting of the Vessels;
- (c) a sum equivalent to 5% of the Consideration shall be paid by CA Shipping to Wuchang Shipbuilding upon keel laying of the Vessels;
- (d) a sum equivalent to 5% of the Consideration shall be paid by CA Shipping to Wuchang Shipbuilding upon launching of the Vessels; and
- (e) a sum equivalent to 60% of the Consideration shall be paid by CA Shipping to Wuchang Shipbuilding upon delivery of the Vessels.

Pursuant to the Initial Shipbuilding Contracts/the New Shipbuilding Contracts, all payments made by the buyer (i.e. ASL Shipping and CA Shipping respectively) prior to the delivery of vessels shall be in nature of advance to the shipbuilder (i.e. Wuchang Shipbuilding). In the event the Initial Shipbuilding Contracts/the New Shipbuilding Contracts are justifiably cancelled or rescinded by the buyer in accordance with the terms of the Initial Shipbuilding Contracts/the New Shipbuilding Contracts, the shipbuilder shall refund to the buyer all sums paid to the shipbuilder, together with interest, from the date of receipt by the shipbuilder to the date of remittance. The shipbuilder shall deliver a refund guarantee to the buyer according to the term of Initial Shipbuilding Contracts/the New Shipbuilding Contracts for the aforesaid refund.

As advised by the Management, Wuchang Shipbuilding had yet to deliver the refund guarantee to ASL Shipping. As at the Latest Practicable Date, no instalments of Consideration was paid by ASL Shipping to Wuchang Shipbuilding.



Pursuant to Initial Shipbuilding Contract I, no adjustment to the consideration shall be made for the 60 days of delay in delivery beyond the delivery date as defined in the Initial Shipbuilding Contract I. If the delivery is delayed more than 60 days after the delivery date as defined in the Initial Shipbuilding Contract I, the consideration shall be reduced by US\$5,000 per day (the total reduction shall not be more than 180 days at the specified rate of reduction from the 61st day after the delivery date as defined in the Initial Shipbuilding Contract I). If the delay in delivery continues for a period of 240 days after the delivery date as defined in the Initial Shipbuilding Contract I, the buyer may terminate the Initial Shipbuilding Contract I according to the terms therein.

Pursuant to Initial Shipbuilding Contract II/the New Shipbuilding Contract I/the New Shipbuilding Contract II, no adjustment to the consideration shall be made for the 30 days of delay in delivery beyond the delivery date as defined in the Initial Shipbuilding Contract II/the New Shipbuilding Contract I/the New Shipbuilding Contract II. If the delivery is delayed more than 30 days after the delivery date as defined in the Initial Shipbuilding Contract II/the New Shipbuilding Contract I/the New Shipbuilding Contract II, the consideration shall be reduced by US\$5,000 per day (the total reduction shall not be more than 180 days at the specified rate of reduction from the 31st day after the delivery date as defined in the Initial Shipbuilding Contract II/the New Shipbuilding Contract I/the New Shipbuilding Contract II). If the delay in delivery continues for a period of 210 days after the delivery date as defined in the Initial Shipbuilding Contract II/the New Shipbuilding Contract I/the New Shipbuilding Contract II, the buyer may terminate the Initial Shipbuilding Contract II/the New Shipbuilding Contract I/the New Shipbuilding Contract II according to the terms therein.



Analysis on the consideration

Under the Proposed Acquisition, the consideration shall be paid by the buyer to the shipbuilder in instalments according to the shipbuilding progress of vessels, with majority of the consideration payable on the delivery of vessels. As advised by the Management, such payment schedule (i.e. payment in instalments according to the shipbuilding progress with majority of the consideration payable on the delivery of vessels) was determined based on arm's length negotiation with the shipbuilder; and was in line with market practice. For our due diligence purpose, we have identified transactions in relation to the acquisition of vessels from shipbuilders announced/conducted by companies listed on the Stock Exchange during one year prior to the announcement of Proposed Acquisition dated 18 May 2022 (the "**Market Transactions**"). To the best of our knowledge and as far as we are aware of, we found 12 transactions which met the aforesaid criteria. We consider the one-year period to be fair and reasonable as it can demonstrate the trend of transactions of similar nature as the Proposed Acquisition conducted by companies under proximate timeframe prior to the entering into of the Proposed Acquisition. Accordingly, we also consider the Market Transactions to be fair and representative for our analysis. We noted from the Market Transactions that, (i) the purchase price of vessels are paid according to the agreed milestones of the shipbuilding progress; and (ii) in 9 out of 10 Market Transactions (excluding two transactions with no disclosure on detailed payment schedule), majority of the consideration is payable on the delivery of vessels. Accordingly, we are of the view that the payment terms of the Proposed Acquisition are fair and reasonable.

For our due diligence purpose, we enquired of the Management the internal procedures of the Group in relation to the purchase of vessels for leasing purpose. As advised by the Management, for the Group's leasing projects, the business department shall prepare the relevant project reports and/or other supporting documents (such as price justification documents) for the assessment of the risk management department; and the projects shall be reviewed and approved by the Board/general manager's committee (which is a committee comprising the Company's managers and chaired by the Company's general manager). The project reports and/or the relevant supporting documents include relevant assessment of the leasing project, such as analyses of the vessel purchase prices. When preparing the project reports and the relevant supporting documents, the business department would refer to, among other things, prevailing market values for the construction of similar vessels, as ascertained from industry reports prepared by research companies and/or recent comparable transactions in the industry announced by Clarkson (the "**Internal Procedures**").



The Management confirmed that the Company followed the Internal Procedures when entering into the Proposed Acquisition. For our due diligence purpose, we obtained from the Company internal price justification document in relation to the Proposed Acquisition. We noted from such document that the Company considered, among other things, (i) newbuilding prices for feeder container ships as published by Clarkson; and (ii) the shipbuilding price quotes from other shipbuilders which ranged from US\$23.5 million to US\$24 million. We also obtained a publication by Clarkson dated April 2022 which the Company made reference to when preparing the price justification document. According to such publication, the market newbuilding price for comparable container ships was approximately US\$23.5 million at the end of 2021 and approximately US\$24.3 million in March 2022. In addition, according to Clarkson's data, the market newbuilding price for comparable container ships was US\$24.5 million in April 2022. The purchase price of the Vessels of US\$22.98 million each was lower than the aforesaid recent newbuilding price in the market. Having considered (i) the aforesaid background of Clarkson; and (ii) the aforesaid data from Clarkson represents the market shipbuilding prices, we consider it is fair and reasonable to make reference to the Clarkson's data. Accordingly, we are also of the view that the Consideration of the Proposed Acquisition is fair and reasonable.

Having considered the above, we are of the view that the terms of the Proposed Acquisition are fair and reasonable

4. Possible financial effects of the Proposed Acquisition

According to the Board Letter, it is currently expected that 25% of the Consideration of the Proposed Acquisition will be funded by shareholders' loan provided by the shareholders of CA Shipping or its nominees (as the case may be) and 75% of the Consideration of the Proposed Acquisition will be funded by the banking facilities to be obtained by CA Shipping. The Company shall provide such shareholders' loan to CA Shipping in proportion to its shareholding in CA Shipping by using its internal resources. If the bank requires the shareholders of CA Shipping or its nominees (as the case may be) to provide guarantees and/or collaterals, the Company shall provide such guarantee and/or collaterals in proportion to its shareholding percentage in such entity. As advised by the Management, CA Shipping will liaise with the banks regarding the bank facilities and terms of such bank financing will be determined subject to negotiation between CA Shipping and the bank. When determining the terms of the bank financing, CA Shipping would refer to the term of the relevant vessel lease.

As advised by the Management, the Group's bank borrowings mainly represent bank financing for the construction of vessels in its ordinary and usual course of business. For illustration purpose only, according to the 2021 annual report of the Company, the Group had bank borrowings of approximately HK\$19.6 billion as at 31 December 2021, with weighted average interest rates ranging from 0.96% to 2.27% per annum.



Upon completion of the Proposed Acquisition and delivery of the Vessels, the Group's fixed assets shall increase by the amount of the Consideration for acquisition; the Group's current assets shall decrease by the amount of the Consideration to be funded by internal resources; and the Group's liabilities shall increase by the amount of the Consideration to be funded by bank financing.

OPINION AND RECOMMENDATION

Having taken into account the above principal factors, we consider that (i) the terms of the Proposed Acquisition are on normal commercial terms and are fair and reasonable; and (ii) the Proposed Acquisition is in the ordinary and usual course of business of the Group and is in the interests of the Company and the Shareholders as a whole. Accordingly, we advise the Independent Board Committee to recommend, and we ourselves recommend, the Independent Shareholders to vote in favour of the relevant ordinary resolution(s) to be proposed at the EGM to approve the Proposed Acquisition.

Yours faithfully,
for and on behalf of
SOMERLEY CAPITAL LIMITED

Clifford Cheng
Director

Mr. Clifford Cheng is a licensed person registered with the Securities and Futures Commission and a responsible officer of Somerley Capital Limited, which is licensed under the SFO to carry out Type 1 (dealing in securities) and Type 6 (advising on corporate finance) regulated activities. He has over ten years of experience in the corporate finance industry.